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Introduction

1. The Regional Consultative Meeting on Financing for Development in the European Region was opened by Danuta Hübner, Executive Secretary of the Economic Commission for Europe (ECE). She emphasized that the main objective of the consultation was to exchange views and experiences in attracting public and private flows to the transition economies and in using them effectively for development. The meeting was also expected to provide regional perspectives on issues related to governance in monetary and financial systems at the global level. She recalled that this meeting was part of the preparatory process towards the High-level International Intergovernmental Event on Financing for Development, to be held in 2002.

2. Jørgen Bøjer (Denmark), Chairman of the Preparatory Committee for the High-level Event, was elected Chairman of the meeting. Mr. Bøjer provided details about the preparations for the High-level Event, pointing, inter alia, to the participation of other regional commissions, United Nations bodies, the International Monetary Fund and the World Bank, as well as entities from civil society and the business community.

Conduct of the meeting

3. The meeting was conducted through a series of panel discussions on five specific themes related to the general problem of financing for development.

4. The present report is based on the views expressed and the suggestions made by panellists, member States, NGOs and representatives of the private business sector. It reflects lessons drawn from experience in the region and presents conclusions that might be usefully taken up in the preparations for the High-level Event. The following is not a text agreed by ECE member Governments but a report of the proceedings prepared by the ECE secretariat. The Chairman's summary is contained in annex I, the programme of the meeting in annex II.

Financing the process of transformation and development in the ECE transition economies

5. The plenary session raised some important points which were taken up in more detail in the subsequent working sessions. It was emphasized that Europe is unique for its wide disparities in levels of economic development across countries. Transition economies have a much lower level of real income per capita than Western European countries, but there are also large disparities in the level of economic development among the transition economies themselves, which underlines the importance of the issues related to financing for development in Europe. A major goal of economic policies is to achieve sustained economic growth and a significant reduction of income disparities between East and West. But experience shows that the process of catching up will take considerable time and that it will require massive restructuring of these economies, pointing to the need for huge investments in physical and human capital, which will have to be financed mainly from domestic resources.

6. It was stressed that many transition economies face chronic economic and social problems which are essentially those of underdevelopment, including very low (by international standards) average levels of real per capita income, widespread poverty, inadequate health-care systems and widening income and social differentiation. The problems of transition, however, are in addition to those of development, and both are compounded by the economic and political consequences of an unprecedented transformational depression, as well as numerous conflicts and even wars in some parts of the region. This is a highly complex mixture of problems, which has exposed these economies and their populations to excessively high levels of strain and suffering.

7. Western donors noted that economic development and its financing remains a crucial issue, and that the process towards the high-level meeting is therefore a very good occasion to single out the key factors for economic development and poverty reduction. They emphasized that domestic factors, especially consistent reform policies designed to achieve broadly based economic and social progress, are of prime importance for the transition process and the process of economic development in general. Development aid has to be seen as a catalyst that facilitates/supports domestic efforts. Attention should be paid to measures designed to increase the efficiency of assistance, including improved coordination among donor countries and international financial institutions (IFIs). It was emphasized that efforts should be made by developed countries to meet as soon as possible the objective to

raise the level of official development assistance (ODA) to 0.7 per cent of their gross domestic product (GDP). In view of the heterogeneity of levels of development and the associated diversity of problems, there is a need to tailor both official assistance and debt relief to the specific needs and circumstances of individual countries. It was also noted that enhanced market access for developing countries' exports is a cornerstone for supporting their economic growth.

Strategies

8. It was pointed out that there is no universal recipe for economic development and catching up with the more developed economies. This depends on a host of factors, the relative importance of which is difficult to quantify. It is therefore difficult to emulate successful development strategies adopted in such countries as Ireland. More generally, the key factor is the domestic absorptive capacity, which in turn depends on such factors as effective institutions, macroeconomic stability, structural reforms, close integration with the international division of labour and the quality of human capital.

9. It was also noted that coherent and consistent reform policies are a conditio sine qua non for successful development. The "old" enterprise sector should face a hard budget constraint and there should be a conducive environment for the creation of new firms, especially small and medium-sized enterprises (SMEs).

Fixed investment and foreign direct investment

10. Fixed investment is the carrier of technical change and is therefore at the heart of the process of creating competitive economic structures in the transition countries. The direction of causality between investment and economic growth is difficult to establish and is best thought of as a mutually reinforcing process. There were concerns that a lack of fixed investment and disappointing rates of economic growth could lead to a loss of human capital in the transition economies, either because of a deterioration of skills associated with high and persistent unemployment or outward migration.

11. Foreign direct investment (FDI) can play an important catalytic role in the transition process: it is a source not only of funds for financing external deficits but also of new technology and know-how.

Domestic and external financing

12. It was noted that transition economies differ widely with regard to their external financing problems. The bulk of domestic investment is, in any case, almost always financed internally.

13. In the leading European Union (EU) accession candidate countries, the main challenge is the savings-investment imbalance. Low domestic savings (partly reflecting demographic factors) contrast with very high investment needs. These partly reflect the need to meet the high standards of the *acquis communautaire* in the fields of energy, environment and transport. But in these countries, (foreign) private capital is increasingly available, thus reducing the need for official bilateral and multilateral assistance.

14. In contrast, in the less developed transition economies the domestic savings base is weak and financial intermediation underdeveloped. Governments face an inadequate domestic revenue base which does not even allow them to fulfil their basic "night watchman" role. Private capital inflows are forthcoming only to a limited extent. These countries continue to rely strongly on official assistance, a main priority of which should be the financing of public infrastructure projects.

Role of official assistance

15. It was emphasized that Western official assistance is essential for the transition process to succeed and to create the basis for a sustained process of economic development. But it was stressed that official assistance can only complement domestic efforts. Western donors, however, should remind themselves that a successful outcome of the transition process is in their self-interest since this will help to ensure the long-term economic and political stability of Europe as a whole. This was one of the lessons to be learned from the Marshall Plan, which represented a realistic and farsighted appraisal of what was required to ensure economic recovery and political stability in Western Europe after the Second World War.

I. Mobilizing financial resources for transformation and development: the domestic dimension

Issues in domestic resources mobilization during economic transformation

16. Mobilizing domestic resources has been important for growth since the time of the industrial revolution because much of the domestic investment that propelled this growth was financed through domestically generated savings. The same is true today, but countries in the Eastern region of ECE are facing exceptionally large social and economic costs associated with economic transformation. Despite an increase in savings during the second half of the 1990s, there appears to be a significant gap between the demand for investment and the availability of domestic resources in the region.

The savings-investment nexus and inadequate financial intermediation

17. It was reported that, according to a recent study made by the ECE secretariat, there is a strong correlation between savings and investment rates across the transition economies. But the role of savings in economic growth is ambiguous in economic theory. Higher savings can translate into higher investment, which in turn leads to higher growth, but higher growth can also stimulate savings (reverse causality). Nevertheless, the high savings and investment ratios observed in most of the countries undergoing economic transformation contrast with a relatively high variance in their economic growth rates.

18. Most of the participants agreed that missing or ineffective institutions appear to be a major reason why domestic savings are not always channelled into investment. Poor regulatory frameworks hinder the development of financial markets, which in turn restrain the mobilization of domestic savings. Poor governance of the banking sector can also hinder investment. The development of real estate markets can make an important contribution to the improvement of intermediation, but these require well-defined property rights. Ineffective financial institutions can lead to a lack of confidence of households and firms, thus enlarging the financial gap.

19. The development of financial systems and capital markets in the transition economies was therefore considered to be very important for the mobilization of private savings. There is strong evidence that countries with more developed financial systems channel more savings into investment. Hence, the acceleration of financial reforms in the transition economies is likely to stimulate private savings and consequently contribute to higher rates of economic growth. In the meantime, if there is a surplus of savings but ineffectual or missing institutions, then the IFIs should step in and mobilize local funds for investment.

20. In addition, there was agreement that the macroeconomic environment also plays an important role in closing the financial gap. Sound macroeconomic policies must be in place for the savings rate to increase, and consistent external and internal policies can also help channel domestic savings to investment.

21. There was also some concern among participants that the region had an unfavourable age structure, that is, an increasing proportion of elderly persons with a low savings propensity. This has important implications for social security. As the population ages, government expenditures for pensions tend to rise as a percentage of GDP. This will, ceteris paribus, lead to lower national savings rates. There is also evidence that people do not save in the prime of their lives as suggested by the life-cycle hypothesis.

Finance for SMEs

22. It was considered important to ensure a conducive environment for the financing of SMEs. Foreign bank loans are typically channelled towards the more profitable sectors, which do not generally include SMEs. Despite support for SMEs by the international lending institutions, local banks do not provide support for SMEs because of missing institutions, poor governance or lack of competence. Nevertheless, SMEs are thriving in some countries because the bulk of their investments is self-financed.

Public-private partnerships

23. Governments and official institutions can mobilize local private resources to finance commercially viable infrastructure ventures. The direct effects include the utilization of the local labour force, the mobilization of other local resources, the sharing of risk between government and the private sector, and the use of local professional advice (legal, technical etc.).

Revenue for social development

24. There was concern that the current need for domestic resources for economic restructuring might hinder social development in the region; in fact, social problems have to be handled simultaneously with economic ones. Social development is seen as a human investment (in education, health and social services) that not only improves the social welfare of society but also increases the human capital needed to sustain economic growth. In Western Europe, the state, private sector and civil society all provide social welfare, but in the transition economies the role of the state has diminished, the private sector is only just emerging (but providing only for those who can pay) and civil society is not yet ready to accept such responsibility.

Concluding observations

25. External financing, such as FDI, appears to be an important factor for stimulating growth. This may reflect the fact that it is a type of investment that also brings technology and new organizational methods. But empirical research in this area is still limited and existing modelling frameworks are not adequate to establish the scale of these benefits or the conditions which are most likely to give rise to them.

26. However, in general it can be expected that the transition economies will follow the traditional path of primary reliance on their domestic savings as the main source of financing future development and growth. Hence, domestic policy must play a very important role in mobilizing private savings and investment.

II. Role of official assistance in creating the conditions for sustainable development

27. The discussion focused on how official financial institutions could help to create the conditions for sustainable economic growth in the transition economies. At various times during the past decade, these economies have been faced with the simultaneous tasks of macroeconomic stabilization and systemic and structural reform, tasks which have required considerable resources that, at least early in the transition, could not generally be mobilized internally or from private foreign investors. Bilateral and multilateral institutions, including the specially created and transition-oriented European Bank for Reconstruction and Development (EBRD), have sought to fill the gap.

28. Participants agreed that the global supply of official finance (especially ODA) is limited, and that the financing needs of the transition economies would have to be met increasingly from private sources. In fact, due to the improving investment climate in many transition economies, the private sector now represents the major share of capital inflows. As for official funds, it was repeatedly noted that they should act as a catalyst for the development of the private sector and the mobilization of private capital. A number of delegations from countries with transition economies underlined the importance of official assistance in the early phases of the transition process, which had helped them to achieve macroeconomic stabilization and put them on the path to economic recovery. In addition to providing badly needed funds, arrangements with official institutions help to generate confidence in the investor community. However, it was also stressed that official assistance should be viewed as temporary, and that in the longer term it is not a substitute for domestic adjustment, restructuring and the mobilization of local savings. Even as foreign capital inflows increase, domestic savings are expected to provide the bulk of development resources.

Regional heterogeneity and the continuing needs for assistance

29. A major theme was the heterogeneity of the transition countries and their future requirements for official assistance. These large differences are reflected, inter alia, in the levels of income (seven countries are eligible for International Monetary Fund (IMF) poverty reduction and growth arrangements), progress towards stabilization, the stage of economic reform and the degree of access to the international capital markets. There was a consensus that while the need for official assistance has generally diminished, it still has an important role to play in the transition. However, tailoring it to countries' changing needs and sectoral developments remains a challenge.

30. As countries progress towards a more advanced stage of reform, their circumstances and financial needs change and evolve. In the middle-income, advanced transition economies, which have generally been successful in attracting various types of private capital, the IFIs are to continue to foster systemic reforms, finance infrastructure and help, inter alia, with

environmental clean-up and training. It should be borne in mind that access to the international capital markets does not currently guarantee maturities of the duration required for projects with long gestation periods. In the case of the less advanced reforming countries, relatively larger volumes of the more traditional assistance — for economic development, macroeconomic stabilization and structural reform — are still required.

31. *Governments made the following suggestions:*

(a) Official assistance be additional to any funds forthcoming from the private sector. Public funds should not displace private funds;

(b) Official assistance not be withdrawn too quickly since this could endanger other domestic programmes;

(c) Potential recourse to IFIs as a source of emergency stand-by assistance be maintained;

(d) One delegation proposed that the developed countries fulfil their commitment to devote 0.7 per cent of their GDP to providing ODA;

(e) A proposal was made to provide debt relief to several low-income transition economies which appear to have unsustainable debt burdens.

Assistance for sustainable economic growth

32. In addition to providing resources, there was consensus on the proposition that the IFIs should promote policies and long-lasting market reforms which would set the stage for sustainable economic growth. Their classic function of infrastructure financing and its positive externalities were mentioned. However, discussion focused on the fact that the leverage provided by official funds should be used to maximize its "transition impact". Mechanisms or policies which could be used to this end include the judicious application of conditionality, closer interaction between IFIs and the private sector, and the strengthening of market-supporting institutions. In particular:

(a) A number of recipient Governments noted the benefits accruing to them from conditionality (i.e., the terms attached to IFI resources). These benefits — deriving from IFI help with policy and project design, technical assistance, monitoring compliance with programme parameters etc. — were often viewed to be as or more important than the availability of funds;

(b) IFIs should continue work on improving banking, financial, legal and regulatory institutions, but it was felt that it is also important to recognize and address the important political obstacles that have prevented effective action in the past;

(c) The ability of the IFIs to mobilize private funds by lending their name to projects and sharing risks with the private sector was considered a major asset. IFIs can take the lead in projects, regions and countries where the private sector is reluctant to enter;

(d) The involvement of IFIs in projects can provide the basis for the improvement of corporate governance in the host economy.

33. Another beneficial commitment mechanism singled out by recipient countries was the pre-accession negotiation process with the EU. This was regarded as a blueprint for structural reforms, and was considered to supply a crucial motivation for internal adjustments and the introduction of structural measures, such as privatization and deregulation, as well as enhancing their sustainability. The pre-accession programmes have been financed by various EU funds and technical assistance.

34. IFIs have been instrumental in supporting the development of SMEs through loans, equity participation and policy advice. In addition to their key role in economic recovery — an observation made by some speakers — the role of SMEs in the development of civil society and open markets was seen as essential for the evolution of an efficient market system.

35. *Governments suggested that:*

(a) The effectiveness of conditionality can be further increased if more efforts are made to customize it to country-specific circumstances. Where it isn't already practised, a policy dialogue between donor and recipient is desirable;

(b) Competition among IFIs and other official donors to soften conditionality should be avoided since it is likely to result in the postponement of necessary reforms, with long-term negative consequences for the recipient countries;

(c) Competition between donors can lead to excessive and sub-optimal grant elements, which also reduce the aid available for other recipients;

(d) Public private partnerships (PPPs) should be further explored as a means of mobilizing finance and sharing risk, but some Governments warned that they are not a panacea.

Coordination of aid and regional issues

36. Several issues relating to aid coordination by donors and the need for measures to enhance regional ties were raised in the debate.

37. Although some progress has been made in the coordination of assistance between donors (multilateral and bilateral), participants felt that further improvements were desirable. Coordination is difficult because of the differing objectives of multiple donors, donors' differing assessments of country needs and differing national aid preferences. However, one participant noted that the lack of experience in the area of aid administration meant that the transition economies sometimes had difficulties in using aid efficiently. Another drew attention to the fact that disbursement of aid has often been delayed.

38. More effective regional cooperation could bring benefits to certain areas in the ECE region. This is especially true of trade and infrastructure because economic relations under the former economic system were shaped by Governments rather than by market forces and comparative advantage. In this area, too, some progress has been made, but it was agreed that more needs to be done. Many of the countries in South-East Europe provide the latest challenge for such a new approach.

III. Foreign direct investment and the restructuring of transition and emerging economies

39. FDI was regarded as a major source of funds in closing the financing gaps of the transition economies. However, FDI inflows into the transition economies have been relatively weak (with a few exceptions) and highly differentiated across countries. The major impediments to a faster growth of FDI in the transition economies are the lack of or weak implementation of necessary policies (which may have been already passed by legislatures) and the rather low responsiveness of domestic agents (weak capacity of a society to adjust to the new market environment).

40. The current situation in the transition economies reveals several important patterns of FDI and its impact:

(a) The distribution of the FDI stock accumulated during the last 10 years among the recipient countries is rather diversified. In terms of the total stock, the bulk of FDI is concentrated in four or five transition economies. While the Russian Federation is included in this list, it ranks nearly last in terms of FDI per capita;

(b) FDI inflows as a percentage of the stock of fixed capital in the transition economies also vary, but less considerably, and even in the most successful countries it is less than 10 per cent of the total stock, indicating that even in these countries FDI is not the main source of capital formation;

(c) The observed performance in the manufacturing sector reveals higher productivity, stronger export orientation and a high rate of reinvestment capacity in firms with foreign participation. There is also strong evidence of an increasing gap between the performance of foreign and domestic enterprises within the same industry and also within the same country;

(d) A side-effect of foreign takeovers (in particular by transnational corporations), which sometimes has a negative impact on public opinion, has been the conversion of independent domestic companies into subsidiaries of foreign concerns, which implies a certain loss of sovereignty in decision-making and entry into a different sphere of competition (mainly within the multinational corporations distribution networks);

(e) Government policies related to FDI differ among recipient countries in a number of ways. These include: methods of privatization (scope and terms); national treatment (incentives for FDI or non-discriminatory); potential bias towards big investors, hence FDI; and incentives for start-ups or greenfield investments. However, investment promotion (both domestic and foreign) in the transition economies often faces budgetary constraints due to the low levels of public revenue.

41. Considerable attention was devoted to public policy issues, in particular those related to FDI. The central question was which policies were more efficient in attracting FDI, in particular what should be the role

of incentives, if any, in stimulating inward investment. There was consensus among the participants that the keys to success are: (a) consistent and coherent economic policies, and (b) a generally favourable environment for business investment (both foreign and domestic). Policies aimed at providing selective incentives to foreign investors created distortions in the economy and were not considered efficient in terms of social welfare in the long run.

42. The success stories among the transition economies are mostly in countries that have managed to provide a stable environment (both economically and politically) and to maintain consistent, transparent and predictable policies. In turn, microlevel success stories indicate the importance of cooperation and policy consistency between the different levels of government: general, local and municipal. In contrast, the inflow of FDI has been much smaller in countries and regions characterized by political and economic instability, crime and corruption, a weak judiciary and poor infrastructure.

43. The experience of some West European countries in instigating FDI-led growth could also be instructive for the transition economies. Thus, Ireland's experience shows that an individual country can do a lot to attract FDI, not only because it could offer relatively easy access to a large market (EU membership), cheap skilled labour and tax incentives but also by consistently delivering on policy commitments (the same policies were pursued over several decades) and by providing supplementary support through related policies (such as education and training and the development of necessary skills) to make those investments long-lasting.

44. One word of caution for the transition economies was that they should take note of the fact that local businesses may not always be interested in promoting FDI since this will increase the competitive pressure they have to face. And when public governance is weak, such interest groups may create serious obstacles to the inflow of FDI. Cartel agreements among local firms and directed against firms with foreign participation are also common in some countries.

45. The transition economies that aspire to EU membership must also gradually harmonize their investment-related policies with those in the EU. Thus, the latter excludes the granting of special privileges to foreign investors, or for that matter to any selected group of businesses. Therefore, some of the special incentives that are in place in some countries (such as duty-free zones, tax holidays and the like) will need to be gradually phased out.

46. It was pointed out during the discussion that while most of the attention has been focused on the policies of recipient countries, there has been considerably less debate on the policies related to outward investment in the countries of origin: there are considerable divergencies among these which may also create distortions. It was felt that there is a need for more cooperation and exchange of information in this field in order to achieve greater uniformity and cohesion.

47. Internationally agreed trade-related policies and rules, in particular in the context of the World Trade Organization (WTO), also have an important impact on FDI, but in terms of policies strictly related to inward and outward investment, progress has been limited. Within the WTO-led negotiations, there have been some attempts during the last three years to unify the international rules that apply to FDI (and to some extent to portfolio investments by foreign agents), and there are some internationally agreed rules on trade in services which partially cover aspects related to foreign investment.

48. Another issue which was debated during the meeting was that of the spillover effects and backward linkages of FDI. It was pointed out that these spillovers are widely considered to be positive (diffusion of new technologies, know-how, managerial skills), but some participants stressed that they can also be negative (the emergence of a dual economy with enclaves of high productivity surrounded by unrestructured sectors of the economy). Policy should aim at maximizing the positive spillovers and minimizing the negative ones. Participants considered that the international community could also do more in this respect by maintaining a regular dialogue between Governments, the private sector, NGOs and other bodies, and by actively disseminating information about best practices and success stories. It was suggested that the business community be involved in discussions during the preparatory phase of the High-level Meeting and be invited to participate in it.

IV. A regional perspective on global financial issues

49. The benefits derived from the mobilization of scarce financial resources — via international capital flowing to the most productive uses — have contributed to economic growth and increased standards of living in all regions of the world.

50. But the recent financial crises in Asia and the Russian Federation have also shown that international capital movements are inherently instable and can trigger severe financial (banking, currency, debt) crises, with attendant severe economic and social costs. In view of their strong dependence on foreign capital, developing countries and transition economies are especially vulnerable to the excessive volatility of such flows. Efforts to mitigate or prevent such financial crises should therefore be at the top of the policy agenda. This is all the more urgent because such crises reflect the impact of both policy failures and market failures.

51. While there is no general agreement as to the future international financial architecture, there is, nevertheless, a general acceptance of the clear responsibility of domestic policy makers to create a sound legal and regulatory framework for the optimal working of markets. International reform efforts are important but are no substitute for sound domestic economic policies.

Codes and standards

52. Codes and standards for improving the quality and timeliness of information concerning major macroeconomic variables and the reporting of financial and non-financial firms were regarded as a necessary condition for allowing more rational decision-making by lenders and investors. It was noted that such standards as the IMF Special Data Dissemination Standard can help central banks to identify data needs. Increased transparency should also allow markets to exercise greater discipline over policy makers and strengthen policy surveillance by the IFIs. Progress in this area has been uneven. It was noted that less progress has been made in the financial reporting of banks and other financial institutions than in the public sector. It was emphasized, however, that global standards and codes should not become straitjackets but rather serve as broad guidelines which should allow for the diversity of countries in terms of development level, history, culture etc.

Financial regulation and supervision

53. The strengthening and restructuring of the financial sector will not be possible without a coherent national regulatory framework. Regulatory reform is therefore a necessary condition for reducing the probability of financial crises and, when they occur, limiting their adverse effects. It was also stressed that there is scope for improving the coordination between national regulatory authorities, particularly in the area of data exchange. There was a consensus that a global regulatory institution (World Financial Authority) is unlikely to be more effective than the coordinated efforts of national authorities in applying global standards.

Conditionality

54. The overriding principle of IFI assistance, including in the field of finance, must be "country ownership". Conditionality is an essential part of concessional lending, but the nature of conditionality should be reviewed in the context of prevailing domestic economic fundamentals, which will differ across countries. It was noted that conditionality is an important indicator for private investors and lenders.

Capital account liberalization

55. It was acknowledged that "boom-bust cycles" in short-term capital flows can create serious problems for macroeconomic management and financial supervision in the transition economies and other emerging markets. It was suggested that controls on private short-term capital flows may be necessary for reducing excessive volatility and thus ensuring greater stability of the financial system. Such controls should be market-based instruments (e.g., taxes, minimum reserve requirements) and are best seen as complementary to regulatory reform and supervision as well as to increased transparency regarding the activities of Governments, financial institutions and private enterprises.

56. Some participants believed capital controls to be measures to which resort should only be made in case of emergency; others regarded them as essential for economies with fragile financial systems. In any case, capital account liberalization should only occur as the

culmination of a carefully sequenced process of economic reforms and strengthening of domestic financial institutions.

Exchange rate arrangements

57. The general view was that exchange rate regimes cannot be discussed independently of the underlying capital account regime. Any recommendations for exchange rate regimes have to take into account the economic conditions in each individual country. Given that these differ, the appropriate regime will also differ across countries.

58. Between the extremes of freely floating exchange rates on the one hand and strictly fixed exchange rates on the other, there exists a range of intermediate solutions which may fit the specific circumstances of individual countries.

59. It was noted that the instability of freely floating exchange rates can have severe macroeconomic costs in the event of major misalignments. In a region with relatively strong mutual trade links among its constituent economies, an arrangement which aims to limit exchange rate fluctuations (such as the exchange rate mechanism in Western Europe) may be useful but will also require policies to promote real convergence among its members.

60. It was also suggested that the choice of a particular exchange rate and capital account regime not become part of the IMF's conditionality.

V. Conclusion

61. At the closing session, the Chairman presented his conclusions, which were subsequently distributed by him to member States (see Chairman's summary in annex I below). The Chairmen of the working sessions reported briefly on the discussions of their respective subjects along the lines given above. The Executive Secretary of ECE made a closing statement, in which she emphasized that the transition economies in the ECE region had had a decade of experience in dealing with the problems of financing their development, and the meeting had provided an opportunity to draw lessons from success stories and from mistakes.

62. Among the many issues on which she concluded there was general agreement is the importance of mobilizing domestic resources for development, as well as the need to support national efforts with a conducive and enabling international environment. The key role of effective institutions was repeatedly emphasized, as was the importance of implementing agreed rules and policies. The complementarity of all the various forms of finance was stressed, and while agreeing on the importance of private investment, the continuing relevance of public funds in playing a catalytic role was also underlined. Another important theme was the need to deal with the social costs of transition, not only on grounds of social justice but also to avoid social discontent undermining the transition process itself. Reducing government expenditure on unproductive subsidies to inefficient enterprises was obviously necessary, but the resources released could be productively used to support well targeted social expenditure. The important role of the local level with regard to financing for development was stressed, as well as the fact that state decentralization reforms could be seen as a catalyst for a larger active participation of the local community in regional development projects. The necessity to generate new and innovative forms of financing was also emphasized. Another point on which there was agreement was the need for close regional and subregional cooperation as a means of optimizing the use of limited resources. The positive role of conditionality was also recognized, but it was stressed that donors and recipients should enter into a constructive dialogue so that eventually conditionality would be subsumed into an effective partnership. The Executive Secretary also highlighted the considerable diversity of Europe, which in turn underlined the need for partnerships between all the actors involved, from Governments to private enterprises and NGOs etc., and the importance of maintaining a dialogue on all the issues affecting the economic and social development of the region. From this perspective, the meeting had made a constructive and significant contribution.

Annex I

Chairman's summary

Representatives of the member States of ECE and of the Bank for International Settlements (BIS), the European Community, the European Investment Bank (EIB), EBRD, the United Nations Conference on Trade and Development (UNCTAD), the World Bank, IMF and several commercial banks, private companies and NGOs met in Geneva on 6 and 7 December 2000, for a regional consultation meeting, as requested by the Preparatory Committee for the High-level International Intergovernmental Event on Financing for Development, to:

(a) Exchange views and experiences on attracting foreign and domestic public and private financial resources in transition economies and using them for development;

(b) Highlight the lessons and conclusions which could usefully be taken up in the overall substantive preparatory process leading up to the High-level Event, as well as their shared views and ideas on the global aspects of financing for development, with which they can contribute to promoting the overall financing for development process.

Participants noted that their heads of State and Government, in the Millennium Declaration of 8 September 2000 (General Assembly resolution 55/2), had resolved, inter alia, to create an environment — at the national and global levels alike — which is conducive to development and to poverty elimination; had expressed concern about the obstacles that developing countries face in mobilizing the resources needed to finance their development; and had therefore committed their Governments to make every effort to ensure the success of the High-level Event.

It was recognized that the ECE region has a vast and varied fund of experience, particularly from the last 10 years, but also from the post-war years of reconstruction, that is relevant to the work of the financing for development process. This experience highlights the diversity of the situation of individual countries — calling for diversity in ways of addressing their situation — and illustrates the fact that broad local ownership of development strategies is the key to success of development policies.

Staying focused on the need to enhance governance and putting in place domestic policies and regulatory frameworks conducive to savings and investment, including foreign investment, was thought to be important to growth and social advancement. In this regard, many considered the advice contained in adjustment arrangements of the IFIs to be important. There was general agreement on the cardinal importance of supporting the development of the capacity and institutions necessary for the good functioning of market economies, including the ability to ensure sustainability of development from a human and social perspective through a fair social distribution of the development outcome.

Corporate governance was believed to be an area in need of special attention, as was the development of domestic financial sectors. Furthermore, SMEs were seen to have a strong role to play in sustaining and broadening growth and in providing a conducive economic environment and a constituency for reform. It would also be fundamental to bring the knowledge, innovative spirit and capital of informal entrepreneurs into the mainstream of development.

Regional cooperation was highlighted throughout the meeting as crucial to enabling developing and transition countries to enter the global economy and to stimulating foreign direct investments, and as a determining factor contributing to peace, conflict prevention and reconstruction. The Stability Pact aimed at assisting the countries in South-East Europe to cope with the effects of war and the need for peace-building and reconstruction was emphasized by several as an example of such cooperation, but it was stressed that it had been preceded by many others, such as the Central European Initiative.

There was general agreement that a more open and accessible trade environment, providing access for the least developed countries to the markets of the developed countries, is key to their integration into the international trading system and to the success of their efforts to combat poverty.

It was agreed that a stronger effort was needed to prevent financial instability and crisis. A less rigid understanding of the right approach to capital account

liberalization and choice of currency regime seemed to be emerging. Access to capital markets was a key to development in the longer run. However, it should be recognized that markets were volatile and access consequently not guaranteed.

Greater mobilization of resources and more effective cooperation are keys to achieving the international development goals endorsed by the international community. There was widespread agreement that more genuine collaboration among the various partners in development, such as Governments, the United Nations system, the Bretton Woods institutions and the regional development banks, as well as non-governmental organizations and the private sector — which is the essence of the financing for development process — was required to meet the goal. Attention was drawn to the special value of the participatory approach followed by EBRD and others. The United Nations Development Assistance Framework, the comprehensive development framework and the poverty reduction strategy papers were mentioned as timely and appropriate types of instruments aimed at fostering a spirit of cooperation.

Cooperation, however, must respect the diversity of situations and of cultural and historic backgrounds. Many participants pointed to the need for a properly customized and phased approach to development cooperation. Several representatives also underlined the need for external partners to stay engaged and not withdraw from countries too early since this might put achievements into jeopardy. Yet, in the longer perspective, assistance should be considered a transitory phenomenon. As countries developed, they themselves should become providers of support to less advanced nations.

It was recognized that ODA remains an indispensable component of development finance. Representatives of the donor countries committed to the 0.7 per cent of GDP target for ODA reaffirmed their commitment to reach this target as soon as possible. ODA is additional and complementary to national resources. The view that ODA should play a catalytic role in mobilizing private resources, including foreign direct investment, was widely held. Selectivity was also considered a precondition to the effectiveness of assistance, with such criteria as the quality of policy, the opportunity for making a difference and the availability of funding from other sources being mentioned by participants.

Timely implementation of the heavily indebted poor countries (HIPC) initiative is fundamental to enabling countries concerned to set aside sufficient resources for poverty reduction and investment in the social sectors.

With respect to middle-income countries, it was found desirable to concentrate efforts in countries where the proportion of the population below the poverty line remains high.

The financing for development process should be an occasion not only for mobilizing resources for development but also for taking stock of the goals formulated by the United Nations conferences on sustainable development of the 1990s.

Participants saw the financing for development process and the High-level Event as a unique opportunity to strengthen the international community's understanding of a number of factors essential to development and poverty reduction. It was seen as a response to the necessity for greater coherence in policies and among actors at both the national and international levels, representing a comprehensive approach that takes all policies into account, with particular regard to financing and trade.

The Financing for development process holds the potential of developing coordinated leadership for the promotion of sustainable human and social development on an equitable and participatory basis.

By uniting all major actors and stakeholders around a shared analysis of how financing for development can be achieved, a shared sense of purpose and of direction can provide a strong and continuous motivation for political and economic action with the involvement of all for the benefit of all.

Annex II

Programme of the meeting[1]

WEDNESDAY, 6 DECEMBER 2000

Salle XIX

10.00 – 13.00 Opening Plenary Session: Financing the Process of Transformation and Development in the ECE Transition Economies: What are the Main Problems?

Welcome address: Danuta Hübner, Executive Secretary, **United Nations Economic Commission for Europe (UN/ECE)**

Chair of the Session[2]: ***Jørgen Bøjer, Chairman,*** *Preparatory Committee of the High-level International Intergovernmental Event on Financing for Development*

Panel Discussion:
Ignacio Garrido, Vice-Governor, *Council of Europe Development Bank*
Lambe Arnaudov, Deputy Minister for Economy, *Former Yugoslav Republic of Macedonia*
Willem Buiter, Chief Economist, *European Bank for Reconstruction and Development (EBRD)*
Danuta Hübner, Executive Secretary, *United Nations Economic Commission for Europe (UN/ECE)*
Harald Kreid, Chairman, *United Nations Economic Commission for Europe*
Marcelo Selowsky, Chief Economist for the Europe and Central Asia Region, *The World Bank*
Michael Tutty, Vice-President, *European Investment Bank (EIB)*
Alexei Ulyukaev, First Deputy Minister of Finance, *Russian Federation*

Session I and II (held in parallel)

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1 As mandated by the UN General Assembly, this regional intergovernmental meeting is organised in preparation for the High Level Intergovernmental Event on Financing for Development, planned in 2001.

2 Nominated and elected as the Chair of the Conference

Salle XXIII

Special Session I: Mobilizing Financial Resources for Transformation and Development The Domestic Dimension

Chair of the Session[3]: ***Armen Martirossian, Deputy Minister of Foreign Affairs**, Armenia*

Introductory Speaker: ***Péter Ákos Bod, Professor,** Budapest University of Economics, Hungary, **Former President of the National Bank of Hungary***

Discussion Leaders:
***Winfried Braumann, Managing Director,** FGC, Austria*
***Christopher Clement-Davis,** UN/ECE BOT Group*
***Rumen Dobrinsky, Acting Chief,** Transition Economies Section, Economic Analysis Division, Economic Commission for Europe (UN/ECE)*
***Arif Erden, Deputy Director General, General Directorate of Foreign Economic Relations, Undersecretariat of Treasury**, Turkey*
***Robert Hall, Chairman**, (UN/ECE Real Estate Advisory Group)*
***Velimir Rajkovic, Assistant Minister for Finance,** Croatia*
***Nigel Tarling, Director of Programmes,** International Council on Social Welfare*
***Adalbert Winkler, Chief Economist,** German Consulting Company in Financial Sector Development, Germany*
***Olexander S. Yaremenko, Adviser to the Prime Minister,** Ukraine*

Salle XXI

Special Session II: Role of Official Assistance in Creating the Conditions for Sustainable Development

Chair of the Session[3]: ***Cristian Popa, Deputy Governor,** National Bank of Romania*
Introductory Speaker: ***Marie Lavigne, Professor, University of Pau,** France*
Discussion Leaders:
***Manuel Pedro Baganha, Secretary of State of Treasure and Finance**, Portugal*
***Urs Breiter, Minister, Deputy Head,** Division for the Cooperation with Eastern Europe and CIS, Swiss Agency for Development and Cooperation, Swiss Foreign Ministry, Switzerland*
***Christopher Hurst, Head of Division, Chief Economist's Department,** European Investment Bank (EIB)*
***Hans Peter Lankes, Director of Transition Strategy,** European Bank for Reconstruction and Development (EBRD)*
***Bertrand de Largentaye, Head of Unit,** Directorate General External Relations, European Commission*
***Krzysztof Ners, Deputy Minister of Finance,** Poland*
***Marcelo Selowsky, Chief Economist for the Europe and Central Asia Region,** The World Bank*
***Emirlan Toromyrzaev, First Deputy Minister of Finance,** Kyrgyzstan*
***Roberts Zile, Minister of Special Assignments for Cooperation with International Financial Institutions,** Latvia*

[3] Nominated and elected as Vice-chair of the Conference

THURSDAY, 7 DECEMBER 2000

10.00-13.00 Special Sessions III and IV (held in parallel)

Salle XXIII

Special Session III: FDI and the Restructuring of Transition and Emerging Economies

Chair of the Session[3]: ***Krzysztof Ners, Deputy Minister of Finance,*** *Poland*

Introductory Speaker: ***Gabor Hunya,*** *The Vienna Institute for International Economic Studies(WIIW)*

Discussion Leaders:
Rolf Alter, Co-Chair of Investment Compact Project Team of the Stability Pact, *Organization for Economic Cooperation and Development (OECD)*
Richard Eglin, Director of the Trade and Finance Division, *WTO*
John Fitzgerald, Research Professor, *Economic and Social Research Institute, Dublin*
Jonathan Harris, President, Royal Institute of Chartered Surveyors, *United Kingdom*
Eugenijus Maldeikis, Minister of Economy, *Lithuania*
Aleksei Moiseichikov, Ambassador on Special Commissions, *Belarus*
Signe Ratso, Deputy Secretary General, *Ministry of Economic Affairs, Estonia*
Karl Sauvant, Chief, International Investment, Transnationals and Technology Flows Branch, Division on Investment Technology and Enterprise Development, *United Nations Conference on Trade and Development (UNCTAD)*
Joseph Smolik, Chief, International Economic Relations Section Economic Analysis Division, *United Nations Economic Commission for Europe (UN/ECE)*
Vassili N. Takas, Co-Chairman, *Business Advisory Council of South East European Cooperative Initiative, Greece*
Ralf Zeppernick, Director in the Foreign Trade Division, *Ministry of Economy, Germany*

[3] Nominated and elected asVice-chair of the Conference

Salle XXI

Special Session IV: A Regional Perspective on Global Financial Issues

Chair of the Session[3]: ***David Klein, Governor, Central Bank,*** *Israel*
Introductory Speaker: ***Yilmaz Akyüz, Acting Director, Division of Globalization and Development Strategies,*** *United Nations Conference on Trade and Development (UNCTAD)*

Discussion Leaders:
Gunter Baer, Secretary General, *Bank of International Settlements, (BIS)*
Andrew Cornford, Macro-Economic and Development Policies Branch, *United Nations Conference on Trade and Development (UNCTAD)*
Daniel Daianu, Former Minister of Finance, *Romania,* ***National Coordinator of Romania for the OSCE Economic Forum***
Heiner Flassbeck, Macro-Economic and Development Policies Branch, *United Nations Conference on Trade and Development (UNCTAD);* ***Former Deputy Minister of Finance,*** *Germany*
Reinhard Munzberg, Special Representative to the United Nations, *International Monetary Fund (IMF)*
Mosmir Mrak, Professor of Economics, Ljubljana, *Slovenia*
Muravei Radev, Minister of Finance, *Bulgaria*
Alexei Ulyukaev, First Deputy Minister of Finance, *Russian Federation*

Salle XIX

Closing Plenary Session
15.00 – 18.00

Chair of the Session[2]: ***Jørgen Bøjer, Chairman,*** *Preparatory Committee of the High-level International Intergovernmental Event on Financing for Development*

Reports from the Special Sessions:

SSI **Armen Martirossian, Deputy Minister of Foreign Affairs,** *Armenia*
SSII **Cristian Popa, Deputy Governor,** *National Bank of Romania*
SSIII **Krzysztof Ners, Deputy Minister of Finance,** *Poland*
SSIV **David Klein, Governor,** *Central Bank, Israel*

Final Discussion
Closing Remarks
Jørgen Bøjer, Chairman, *Preparatory Committee of the High-level International Intergovernmental Event on Financing for Development,*
Danuta Hübner, Executive Secretary, *United Nations Economic Commission for Europe (UN/ECE)*
Harold Kreid, Chairman, *United Nations Economic Commission for Europe (UN/ECE)*

[2] Nominated and elected as the Chair of the Conference

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Second substantive session
12-23 February 2001

Report of the Regional Consultation on Financing for Development in the Western Asia Region, Beirut, 23 and 24 November 2000

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Introduction

1. The Regional Consultation on Financing for Development for the Western Asia Region was held on 23 and 24 November 2000 at United Nations House in Beirut. It was placed under the patronage of the Prime Minister of Lebanon, Rafic Hariri, and inaugurated, on his behalf, by his Adviser, Ghazi Al-Youssef. The meeting was attended by delegates of six Economic and Social Commission for Western Asia (ESCWA) member States and six non-Member States of ESCWA, representatives of 13 international organizations and United Nations entities, eight regional intergovernmental and non-governmental organizations, 22 regional academic, research institutions and individual experts, and representatives of three private sector banks. The meeting elected Alain Bifany, Minister of Finance of Lebanon, as Chairperson, and Rajeha Bint Abdel Amir Ben Ali, Under-Secretary for Development Affairs of Oman, as Vice-Chairperson.

2. In his welcoming statement, the Executive Secretary of ESCWA, Hazem El-Beblawi, stressed that the international community needs to secure financial resources in order to benefit from the impressive scientific and technological capacities it possesses and to achieve development for the still underdeveloped populations of the world. He underlined that the object of the International Intergovernmental High-level Event on Financing for Development is to secure the agreement of the international community on terms for maximizing and utilizing available resources. Mr. El-Beblawi emphasized that in discussing the attitude of the ESCWA region towards these terms, some distinguishing regional characteristics must be borne in mind. Thus, while all ESCWA members are developing countries, several are also donors. Hence, a single country may epitomize the whole dynamic of the financing for development process by combining the concerns of developing and donor countries at one and the same time. The Executive Secretary also stressed the need to introduce greater stability in the generation and distribution of resources for development, pointing out the detrimental volatility of oil proceeds that have financed developmental efforts in the ESCWA region in the last few decades.

3. In his inaugural statement, delivered by his Adviser, Mr. Al-Youssef, Prime Minister Hariri expressed appreciation for the role the United Nations has played in reinforcing international cooperation by launching the financing for development process. Taking the example of Lebanon, he mentioned that the role of the state in promoting development is to secure the appropriate environment for enterprises through instituting a modern educational system, securing a skilled labour force, establishing needed infrastructure and enacting enabling laws. This should help in attracting domestic and international financial resources alike. Laying stress on the necessity of aligning domestic and international norms and rules, Prime Minister Hariri also emphasized the importance for ESCWA countries and the Arab region in general of a vast integrated economic zone, with financial and human resources and a market, that can enable them to compete in international markets.

4. The meeting discussed three of the six issues identified by the Preparatory Committee for the High-level Event: (a) "Mobilization of domestic financial resources for development" (see sect. I below); (b) "Mobilization of international financial resources for development: foreign direct investment and other private flows" (see sect. II below); and (c) "Addressing systemic issues: enhancing the coherence and consistency of the international monetary, financial and trading systems in support of development" (see sect. III below). The views and ideas of participants spanned a wide range of attitudes and approaches to development financing. A review of these ideas is set out below, based on the papers on the three issues presented to the meeting, comments of discussants, oral interventions during the sessions and written contributions handed to the ESCWA secretariat by participants. Before undertaking the present review, some observations are in order.

5. First, in the discussion of issues, ESCWA countries have been frequently considered together with the Arab countries in general, whether they are situated in West Asia or Africa. This reflects the regional perspective for considering issues in the Arab world.

6. Second, the interrelationship between issues identified by the Preparatory Committee was obvious. Thus, questions of trade and official development assistance (ODA) have been discussed even though they were not retained as topics for the Regional Meeting. This may explain that participants reiterated the same opinions and views about some issues discussed under each of the three topics.

7. Third and most importantly, the meeting was not confined to discussing the demands to be made on industrialized countries. In fact, it examined to greater lengths approaches and policies that should be adopted by ESCWA countries and the developing world in general.

I. Mobilization of domestic financial resources for development

8. Participants agreed that high growth results in higher rates of savings and hence in increased resources allocated to investment and to growth. In other words, high growth triggers a virtuous cycle of savings, investments and higher growth rates. Policy advice was, therefore, concerned with ensuring that high growth takes place. To this end, optimum utilization of different policy instruments was advocated.

9. In achieving strong growth performance, sound monetary and fiscal policies should be put in place so as to ensure a flexible management of exchange rates and credit, the objective being to counteract the cyclical patterns of trade and investment flows. In this respect, it is necessary to preserve the gains achieved by financial stabilization and to avoid slipping back to fiscal deficits, strains on foreign currency or inflationary pressures. In fact, stable economies are essential to promoting savings and investments of the household and business sectors, in addition to attracting foreign capital. It is recognized that capital flight from the ESCWA region, has been, for decades, a major consequence of the absence of a stable and predictable macroeconomic environment. It is acknowledged, nevertheless, that many Governments in the region have improved their macroeconomic variables over the last decade.

10. Efficient and effective institutions are a guarantee for the sustainability of improvements in the economic and social situations in any individual country. They also raise the level of responsiveness of the private sector to the interrelated fields of investment, employment and exports.

11. Sound, regulated and transparent capital markets are effective instruments for mobilizing domestic resources. Views diverged as to whether high or low interest rates are conducive to expansion in economic activity and, hence, to savings and investment.

12. In periods of reform, in order to foster growth and development, the role of the state is to deftly manipulate the institutional and incentive tools consistent with the market mechanism and the objective of a dynamic and innovative private sector. The state must also use its regulatory power to ensure competition and protect the interests of consumers and workers. To this end, ESCWA countries need to formulate competition policies in order to avoid monopoly practices, especially at a time when privatization reaches large utilities and infrastructure.

13. Global competition and economic integration, on the one hand, and the technological revolution in information and communications technology, on the other, allow for efficient private sector participation in investments in and production and management of most public goods, with important welfare gains for the final consumers of these goods and services.

14. The issue of whether the market is an ideology or a mechanism was debated. One view stressed that it is a mechanism for managing the economy, and therefore consists of a set of incentives and disincentives aimed at orienting the resources of a society in a given direction.

15. The issue of equity in maximizing the domestic financial resources that should be directed to development was raised. A question was asked about whether their source should be labour or rather capital. This was considered as closely related to the social orientation of development. Greater equality in the distribution of wealth and income was underscored. Some participants emphasized that it is correlated with growth in savings and the mobilization of domestic resources.

16. Closely linked to the former point was the discussion of the liberalization of labour markets. The reduction in the bargaining power of trade unions and workers associations vis-à-vis employers would result in the redistribution of national income in favour of capital. This could arouse sentiments of injustice and cause social and political disturbances greatly detrimental to the mobilization of resources and to the whole development process.

17. Also in relation to the same point, the advisability of indirect as opposed to direct taxes was raised. The former, considered by some as more efficient for collection purposes, were seen by others as unfair given their regressive character. The need for an

efficient tax administration and reasonable direct tax rates was stressed.

18. Participants agreed on the need for industrialized countries to facilitate the transfer of technology to developing countries, as this would raise productivity and thus result in increasing the level of domestic resources available for development.

19. With regard to the supply side of domestic resources, their maximization depends on three factors. First is the prioritization of basic education and training that result in a rapid decline in the age structure of the population and a concomitant expansion of manpower. In turn, this means higher income per capita and an increased ability to save. Second is the adoption of an export-oriented and labour-intensive growth strategy that allows all modern and traditional sectors, including microenterprises, to become integrated in the process of investment, trade and employment. Third is the implementation of an elaborate industrial policy that combines support for innovation and expansion in the dynamic skill and technology-intensive sectors, with incentives for the traditional labour-intensive sectors that induce them to upgrade skills and adopt better organization, management and marketing techniques.

20. Almost all countries in the region have introduced vast improvements in their investment environments in the past decades, by offering increased incentives, streamlining investment procedures and emphasizing the important role that the private sector can play in raising the levels of private investment. Incentives are fiscal as well as financial and technical. Fiscal incentives include reducing corporate income taxes, providing tax holidays, permitting losses incurred during periods of tax holidays to be written off against future profits, accelerating depreciation allowances, and reducing social security contributions and corporate income taxes charged against marketing and promotional expenditures. Financial incentives and technical assistance include providing subsidized loans, loan guarantees and subsidies to cover part of the capital, production or marketing costs of investment projects. They also involve guaranteeing export credits, providing venture capital for high-risk investments, subsidizing services, such as carrying out feasibility studies, the identification of sources of finance, the implementation and management of projects, and assisting in training and retraining.

21. In spite of the indicated improvements, some participants considered that the level of incentives was insufficient in ESCWA countries. Others stressed that, rather than being across-the-board, incentives should be targeted on specific projects or enterprises. They could also be given post facto, in other words after the activity has taken place successfully. Similarly, tax exemptions could be linked to the achievement of specific, previously established objectives.

22. Maximizing savings, investments, growth and development is correlated with the existence of an enabling institutional framework. An effective legal framework results in lower transaction costs by establishing unambiguous rules on property rights and providing mechanisms for contract enforcement and dispute settlement.

23. Efforts should be geared towards developing savings instruments, such as diversified banking services, postal savings systems and pension funds oriented towards sophisticated financial markets. The latter exist when financial institutions are solid and the range and availability of financial assets are wide. Central Bank regulations should not result in distorting the operation of financial markets and financial repression. However, despite the negative effects on savings, investment and growth of financial repression, financial liberalization should be regarded with caution. In fact, in the absence of institutional structures and adequate standards of accounting and auditing to prevent bad loans, financial distress can result from market imperfections and from competition between banks and other financial institutions.

24. The banking sector being the most important channel for mobilizing savings in the ESCWA countries, exceeding by far the financial intermediation role of banking sectors in industrialized countries, a robust regulatory framework that addresses its specific activities should be put in place. It is noteworthy that, as cross-country studies suggest, a healthy banking sector has beneficial effects on capital accumulation, productivity and economic growth.

25. Trade policy should contribute to growth and increased mobilized domestic resources. Despite recent reforms in the ESCWA region, tariff burdens remain high in several countries and non-tariff barriers pose significant difficulties for international and regional trade. High tariffs and administrative restraints also raise the inputs costs of production for export and

indirectly put pressure on the real exchange rate. This situation should be remedied. In addition, customs valuation and standardization should be simplified and international norms adopted. At the same time, it should be noted that the liberalization of international trade would result in reducing state revenues. This could reduce domestic resources available for development, at least for a certain period of time, and should thus be remedied by appropriate internal and international measures.

26. Also with regard to trade, it was pointed out that in a resource balance equation perspective, the savings gap equals the trade gap, hence the importance of the exchange rate as a tool affecting the savings rate. In the absence of equilibrium, resources could be mainly allocated to the production of non-tradables, thus enlarging the trade gap. A decline in the savings rate would ensue.

27. In the light of the above, for trade to generate resources required for development better coordination between the trade and investment regimes is necessary. This coordination should help ESCWA economies provide profitable domestic investment opportunities in tradable goods and services, and thus encourage the private sector to increasingly shift its activities away from inward-oriented investment, such as construction, real estate and protected manufacturing, towards exports and import substitution on a wide scale, as well as in favour of new dynamic products with high-growth prospects.

28. Also in relation with trade, participants stressed the need for industrialized countries to open their markets to goods and services exported by developing countries with a view to assisting them in increasing their foreign exchange revenues that could be allocated to development efforts.

29. The potential for the involvement of the private sector in investments in and privatization of infrastructure is large but not exploited. This involvement should be promoted. Apart from productivity gains and improved efficiency, it should boost government revenue and release public resources that can be directed to social sectors.

30. Institutional reform, incentives policies and restructuring programmes should also target small and microenterprises and entrepreneurs in the informal sector. This should contribute to realizing the goal of growth with equity, the parallel expansion of export orientation, together with viable import substitution and balance between technology-intensive and labour-intensive industrialization. Specific measures geared to this sector should include tailor-made programmes of technical extension, training and credit, with special emphasis on female employment.

31. When it comes to the demand side, or resource allocation, such sectors as utilities and infrastructure (roads, telephone and power generation), the social sector (health, education and social security), production sectors (agriculture, mining and manufacturing) and productive services (transport, trade and finance) compete for financing. The distribution between the public and private sectors of the responsibility for such financing and for ownership and operation is the issue at stake.

32. Apart from maintaining a high level of spending on social and human development, the challenge is to improve the returns from such spending. Better basic health services, education and focused vocational training are important for attracting private sector investments and participation in development financing.

II. Mobilization of international financial resources for development: foreign direct investment and other private flows

33. The significant resource gap that the Arab, including ESCWA countries, will experience in the coming decades was generally pointed out. Even though, in one view, international financial resources, including foreign direct investment (FDI), should be discouraged in view of their negative effects, the consensus was that these countries should aim to attract them. In this general perspective, international financial resources and the related changes they would bring about should create a virtuous cycle of development in the region.

34. It was stressed that FDI would contribute to the integration of the region in the world economy. In this regard, the correlation between FDI and trade flows was underscored.

35. The small share of the region, at present, in international financial resources, including FDI, was noted. The underdeveloped state of its capital markets

and regulatory environment were mentioned as an explanation for the region's deprivation of its potential share of these resources. The concentration of flows in a few countries and essentially in one sector, oil, was also noted.

36. The openness of the region to the world economy should help it increase its share of FDI. In order to achieve this openness, an opportune policy framework that creates an appropriate environment should be put in place. It was stressed, however, that the appropriate environment is the same, whether resources to be attracted are domestic or international.

37. Gains accomplished in financial stabilization in the region should be preserved. The importance of a sound macroeconomic framework cannot be overemphasized.

38. Skilled human resources are a key factor in attracting international resources. Hence, raising the educational level of labour forces should be one important aim of national policies. In one view, policies should seek to transform comparative advantage in the region towards skill-based goods.

39. Free-trade agreements with industrialized partners, such as the European Union (EU), and membership in the World Trade Organization (WTO) would expand markets for goods and services produced in the region, and should therefore help in attracting FDI and other international resources to the region.

40. In respect of free-trade agreements, it was emphasized, however, that industrialized countries should refrain from protectionism under different disguises. In other words, they should open their markets to the exports of developing countries, thus allowing them to benefit from sectors where they enjoy a comparative advantage. The importance of agricultural products and textiles in the exports of developing countries, including ESCWA countries, was particularly stressed.

41. With regard to WTO, more equitable agreements that take account of the development needs of developing countries are necessary. This applies to future agreements as well as to already concluded ones. In the latter case, consideration should be given to introducing needed amendments.

42. Financial sector reforms, including in the banking sector and the capital market, are important for attracting international resources.

43. Arab multinationals could be an important tool for promoting FDI among ESCWA countries. The emergence of such multinationals and their enhancement could benefit from the association with established multinationals active in the global economy. Industrialized countries should help in this process by making their markets accessible to goods and services produced by Arab multinationals.

44. FDI should contribute to the transfer of technology to ESCWA countries. However, this has not been necessarily the case so far. To illustrate the latter observation, it was pointed out that after nearly 70 years of FDI in the oil sector, the related technology has not been internalized.

45. To promote the transfer of technology, international measures agreed upon by exporting and importing countries should be adopted. Such measures include improved accessibility to markets of industrialized countries for goods and services produced with the transferred technology.

46. Good corporate governance was stressed as an important factor for attracting FDI.

47. It was underscored that international financial resources, including FDI, should not be confined to achieving economic growth. They should also be used to meet the needs of social development. This is particularly important at a time when such areas as the health sector suffer from the impact of economic reforms and trade liberalization pursuant to WTO agreements.

48. ODA is a form of international financial resource. Industrialized countries are called upon to honour their commitment to the target of 0.7 per cent of gross domestic product (GDP) as ODA to developing countries. They are also invited, in the distribution of their ODA, to give a preferential treatment to developing countries that are not favoured by the transfer of international private resources, including FDI.

III. Addressing systemic issues: enhancing the coherence and consistency of the international monetary, financial and trading systems in support of development

49. The Arab region, including the ESCWA countries, has been spared the ravages of recent financial crises but has also failed to benefit fully from the spreading trend of market liberalization, globalization and world economic integration.

50. It was mentioned that current efforts to reform the international financial system centre on two overriding themes. First is enhanced surveillance and crisis prevention, including better assessment of financial vulnerabilities, the wider use of standards and codes in monetary and fiscal management, the encouragement of more flexible exchange rate regimes, greater transparency, improvement of the quality of data on key indicators and targeted technical assistance.

51. The second theme is crisis resolution and management, through a rationalization of the role of the International Monetary Fund (IMF) by focusing on its core functions and simplifying its facilities structure, streamlining conditionality, greater transparency in the Fund's own operations and stronger safeguards on the use of its resources, wider involvement of stakeholders in the design of adjustment programmes and closer involvement of the private sector in crisis resolution.

52. Continued work on the former two themes and related initiatives should complement and enhance the success of the attention focused by the international financial institutions (IFIs) on the problems of the poorer countries through the poverty reduction and growth facility (PRGF) and heavily indebted poor countries (HIPC) initiatives.

53. Along with other groups of developing countries, the Arab region is marginalized in the discussions on the reform of the international financial system. Despite the current surge of the region on account of recent increases in oil prices, its role in shaping the new financial architecture is likely to remain limited.

54. As the international financial system enhances its surveillance role of member States' policies, the ESCWA countries are required to provide information on their financial sectors, fiscal management and monetary and banking developments. This will make for greater transparency and accountability, thus creating the conditions for sound domestic financial systems.

55. In one view, in order for the region to take part in current efforts to transform the international financial system, the ESCWA countries need to reinforce their growth prospects by improving their international competitiveness and achieving greater interaction with the industrialized and the faster growing regions of the world. This is a condition sine qua non for the region to realistically aspire to enhance its influence and become a more effective participant in the global financial and monetary order.

56. To meet this condition, countries in the region should undertake reform in different areas. First is reform of the state, which must address its size as well as its role. Second, the ESCWA countries, according to this same view, should implement a comprehensive programme of economic liberalization that includes dismantling price distortions, expanding the opportunities for the operation of the markets, a more open trading system, a more flexible exchange rate regime and a macroeconomic policy aiming at price stability. The shift in policy needs to be supported by modern efficient and competent institutions, including an autonomous bureaucracy, an independent judicial system, strong regulatory institutions, accountability and good governance in the business sector. In this view, these reforms can be expected to release resources and bring about their allocation in such a manner as to raise growth on a sustainable basis. In turn, this would enable Governments to increase spending on priority areas for economic and social development.

57. Another approach emphasized that the increased frequency of international currency and financial market crises, including in countries with a record of good governance and macroeconomic discipline, suggests that financial instability is global and systemic. Accordingly, this means that national policy efforts will not be sufficient to deal with the problem, and that there is a need to establish appropriate institutions and mechanisms at the global level. Analysis and actions advocated by this approach are reviewed below. The ESCWA countries have not necessarily experienced the situations dealt with in this analysis. However, they may face them in the future. In addition, irrespective of whether they will experience

them or not, they should have their word in this regard in order to effectively participate in the governance of the international financial system.

58. Greater transparency and disclosure of information are required from the IFIs, particularly IMF, as much as they are from public sectors and financial markets. To improve its transparency, it has been suggested that the prescriptions of IMF be subjected to independent review, for instance by a commission constituted by the United Nations.

59. Greater transparency and disclosure of information are also needed from banks and other financial firms, as well as from highly leveraged institutions and offshore markets. While they are not sufficient to prevent financial crises, disclosure and transparency are necessary conditions for an improved international financial architecture.

60. The current practice in financial regulation and supervision is for the Bank of International Settlements (BIS) to formulate standards expected to be applied by national authorities, rather than to establish a global regulatory agency. There are, however, three sets of problems with this procedure. First, BIS standards do not properly account for risks in international lending. Second, BIS standards are designed to protect the international banking system, not the debtor developing countries. Third, there are potential problems for developing countries in this approach, which applies indiscriminately to all countries irrespective of their levels of development and different institutions. It was advocated that the adoption of such standards should be voluntary and that it should recognize variations among countries. Moreover, the adherence to such standards should not become part of the IMF conditionality.

61. In addition to supervisory reform and transparency, capital controls are increasingly seen as essential for greater stability. There is a broad-based agreement that the boom-bust cycle in private capital flows needs to be moderated. Controlling short-term, liquid capital inflows through market-based measures, such as taxes or reserve requirements, can attain this goal. Control on inflows would reduce the likelihood of a rapid exit. Should a crisis occur, temporary control on outflows could also be very effective.

62. Developing countries, at present, are increasingly advised to choose either freely floating exchange rate policies or to lock in their currencies to one of the major currencies, often the United States dollar. However, differences among pegged, floating and fixed regimes lie less in their ability to prevent damage to the real economy than in the way damage is inflicted. There now is a growing consensus that better management of exchange rates in developing countries requires targeting real exchange rates in combination with the control and regulation of destabilizing capital flows. This is a viable alternative to free floating or to completely surrendering monetary authority to a foreign central bank. Doubt was expressed over the ability of ESCWA and other developing countries to adopt and manage a free-flowing regime. In any case, the adoption of a particular exchange rate regime should not be part of the IMF conditionality for access to international liquidity.

63. In view of the growing size and integration of financial markets, the prevention of a crisis is a concern for many countries and not only for the one immediately affected. Global surveillance of national policies is, therefore, called for. Failure of the IMF surveillance so far is due to serious shortcomings in the existing governance of IMF, particularly its control by industrialized countries. The need for strengthening IMF surveillance of financial sector issues and capital flows has been recognized anew by its Interim Committee in April 1998. A major factor in the failure of IMF surveillance procedures so far has been their unbalanced nature that gives too little recognition to the disproportionately large global impact of monetary policies of major industrialized countries. In fact, financial crises in emerging countries are often connected to major shifts in monetary and exchange rate policies of industrialized countries. Even though these shifts affect their developmental policies, developing countries lack mechanisms under the existing system to redress their negative impact.

64. In the light of the above, it is a fact that governance in macroeconomic and financial issues lags behind that for international trade where mechanisms are part of the WTO regime. To perform needed functions effectively, in addition to the surveillance procedures, it is necessary to reform the governance of the IFIs, including their voting structures and decision-making processes, with a view to bringing about greater participation of developing countries.

65. The practice so far has been to provide assistance coordinated by IMF, to countries facing capital account problems, after the collapse of currencies, in the form

of bail-outs designed to meet the demand of creditors, maintain capital account convertibility and prevent default. Such assistance has been associated with policy conditionality that went at times beyond macroeconomic adjustment. In other words, efforts have aimed at sparing hazard for international lenders and investors by putting the burden on debtors. To redress this situation, in addition to the role of IMF in providing current account financing, ensuring systemic stability also requires contingency financing to countries experiencing payment difficulties linked to the capital account. Issuing reversible special drawing rights (SDRs) for use in the provision of international liquidity could be considered. The terms under which IMF would play the role of lender of last resort should be worked out.

66. In order to complement efforts of IMF and to undertake more adapted action, the idea of establishing or reinforcing and shoring up existing regional monetary institutions was raised. Related to this, coordination of negotiating positions of ESCWA countries in international forums was advocated.

67. To face up to financial crises, funds required for bail-outs have been continuously increasing. In order to secure them, "involving" or "bailing-in" the private sector has been contemplated. Creditors should share in bearing burdens and be made responsible for their actions. Orderly debt workouts, associated with standstill on servicing, could be considered. They may include reorganization of assets and liabilities of the debtor, including extension of maturities, and, where needed, debt-equity conversion and debt write-off. Involuntary mechanisms have been resisted, but it should be emphasized that the need for mandatory provisions has arisen precisely because voluntary approaches have not worked in stemming debt runs. Fearing that mandated automatic triggers could reduce their access to financial markets, developing countries have insisted that they first be introduced in sovereign bonds of industrialized countries.

Annex

Organization of work

Date/session		*Agenda item/programme*
23 November 2000		
Inaugural session	*Item 1*	Welcoming address: Hazem El-Beblawi, Executive Secretary of ESCWA
		Address by the Patron of the meeting: Prime Minister Rafik Hariri or his representative
	Item 2	Election of the President of the meeting
	Item 3	Adoption of the agenda and the organization of work
	Item 4	Election of the Vice-President of the meeting
Panel I	*Item 5*	"Mobilization of domestic financial resources for development"
		Presentation of a paper entitled "Mobilizing domestic financial resources for development", Heba Handoussa, Economic Research Forum for the Arab countries, the Islamic Republic of Iran and Turkey
		Discussant: Kamal Hamdan, Consultation and Research Institute
		General discussion
Panel II	*Item 6*	"Mobilizing international resources for development: foreign direct investment and other private flows"
		Presentation of a paper entitled "Mobilizing capital for Arab economic development, with special reference to the role of FDI", Ali Sadik and Ali. A. Bolbol, Arab Monetary Fund
		Discussant: Zeki Fattah, Economic and Social Commission for Western Asia
		General discussion
24 November 2000		
Panel III	*Item 7*	"Addressing systemic issues: enhancing the coherence and consistency of the international monetary, financial and trading systems in support of development"
		Presentation of a paper entitled "The reform of the international financial system and the Arab region", George T. Abed, International Monetary Fund
		Discussant: Yilmaz Akyüz, United Nations Conference on Trade and Development
		General discussion
Closing session	*Items 8, 9, and 10*	Overview of the discussions: Hazem El-Beblawi, Executive Secretary of ESCWA
		General debate
		Closing of the meeting

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Second substantive session
12-23 February 2001

Report of the Regional Consultation on Financing for Development in the Latin America and the Caribbean Region Bogotá, 9 and 10 November 2000

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I. Introduction

1. The meeting was opened by Clemencia Forero Ucros, Minister for Foreign Affairs (a.i.) of Colombia, and Juan Manuel Santos, Minister of Finance and Public Credit of Colombia. In their statements, the Ministers focused on the role of the Regional Consultation as a forum for discussion and for the adoption of proposals regarding the establishment of a new international financial architecture. They emphasized the high cost of instability and the need for world cooperation on a grand scale in order to convert the financial environment into an engine of development.

2. The Executive Secretary of the Economic Commission for Latin America and the Caribbean (ECLAC), José Antonio Ocampo, and the President of the Inter-American Development Bank (IDB), Enrique V. Iglesias, also addressed the participants at the opening session. The Executive Secretary of ECLAC noted that the challenges arising from the findings presented in the Secretariat's document entitled "Growth with stability: financing for development in the new international context" (see sect. II below) are to raise investment and savings rates, enhance financial development and export growth, and combine those efforts with initiatives at the national level to reduce the excessive vulnerability of the economies in the region to cyclical fluctuations in external financial flows. The external framework should provide access to markets for exports from the region, a new financial architecture capable of substantially reducing capital volatility, and mechanisms to ensure that all developing countries have access to a sufficient volume of external resources under appropriate terms and conditions. He concluded by stressing that the essential components of the new international financial architecture are the appropriate participation of developing countries in the relevant institutions, the maintenance of countries' autonomy over their own development policies, and the decisive role of regional and subregional institutions. The President of the Inter-American Development Bank (IDB) noted that financing for development has been a fundamental element in Latin America during the 1990s, a time when the region continued to rely heavily on external financing and when its access to that financing was very limited and unstable. The financial system must attain reliability, and doing so represents a systemic issue that calls for a systemic solution. He invited participants in the Consultation to discuss the principles of the new international financial architecture: the creation of mechanisms to provide access to liquidity as a means of combating contagion, the avoidance of pro-cyclical forms of regulation on the part of countries providing funding, the reconciliation of the roles of the private sector and of Governments, the rethinking of the new role of international organizations and the democratization of decision-making.

3. The meeting was attended by representatives of 31 States members of ECLAC, three States that are Members of the United Nations but not of ECLAC, 12 United Nations bodies and specialized agencies, six intergovernmental organizations and 10 non-governmental organizations.

4. The representative of Colombia, Jairo Montoya Pedroza, Vice-Minister of Foreign Affairs, served as Chairman; Andrés Valencia, Ambassador of Mexico to Colombia, Juan Gabriel Valdés, Permanent Representative of Chile to the United Nations, and Julian R. Hunte, Permanent Representative of Saint Lucia to the United Nations, served as Deputy Chairpersons; Gert Rosenthal, Permanent Representative of Guatemala to the United Nations, served as Rapporteur.

Organization of work

5. The work was conducted in plenary sessions structured around five thematic panels (the list of panellists is contained in the annex). A group open to all delegations from the Latin American and Caribbean countries was also formed on the first day of the Consultation. This group worked concurrently to prepare the perspective of those countries.

6. A summary of the proposals presented by ECLAC at the meeting is set out in section II below. Section III provides an overview of each of the five thematic panel discussions, covering both the presentations given by the panellists and the observations made by the attending countries. The statement approved by the open-ended drafting group, entitled "Towards the International Intergovernmental High-level Event on Financing for Development: the perspective of Latin America and the Caribbean", is reproduced in section IV. As agreed at the meeting, member States have until 20 January 2001 to submit any comments to the report.

7. The delegations of the United States and of Saint Lucia, the latter acting on behalf of the Caribbean Community, submitted statements, which are contained in section V.

II. Summary of the proposals of the Economic Commission for Latin America and the Caribbean*

8. Throughout the 1990s, our region experienced renewed access to external financing. This paved the way for progress in macroeconomic management, reducing inflation and resuming economic growth. With few exceptions, however, the Latin American and Caribbean countries have failed to achieve the savings and investment rates required to fuel high rates of growth in production. Not only is the average annual growth rate of 3.3 per cent for 1990-2000 lower than the 5.5 per cent figure recorded for the 30 years prior to the debt crisis but it has also fallen short of the 6 per cent rate identified by ECLAC as being necessary in order to meet ambitious goals for economic and social development, particularly with regard to poverty reduction.

9. At the same time, international capital flows have given rise to concern in two areas. First, with the sole exception of foreign direct investment, these flows have been very unstable. This, along with national policies that often accentuate rather than attenuate the cycles of external finance, has been reflected in a strong correlation between capital flows and economic cycles in our countries. Second, a significant group of countries, especially the relatively less developed ones, have been excluded from the more dynamic types of resource flows.

10. These developments pose important challenges which must be faced by all the countries of the region; nevertheless, a positive international context is also needed in order to ensure the success of the countries' efforts. If they are to grow at a rate of about 6 per cent per year, countries must achieve investment rates between four and six points higher than the average levels of the 1990s. In order to avoid exacerbating the existing level of external vulnerability, additional investment financing must come, basically, from a parallel expansion of national savings, and must be accompanied by an adequate level of national financial development in order to ensure that such savings are transferred to productive investment in the most efficient way possible.

11. The ECLAC document stresses the importance of the reinvestment of private enterprises' profits and of public saving in this effort to raise national saving levels. It also underscores the contribution that households and individuals can make to this objective, especially by saving for specific purposes, such as pension funds, housing or education.

12. The dynamic development of the financial system and the capital market demand reliable ground rules and strong regulatory frameworks in order to guarantee the stability of the relevant systems and the adequate protection of savers. In particular, although the region has already taken up the challenge of adopting international standards for financial regulation and supervision, much remains to be done in this area. An essential aspect of this undertaking is the promotion of new agents and instruments to help complete non-existent or underdeveloped segments of the capital and financial markets, including sound secondary markets, investment and risk-capital funds and guarantee funds, credit insurance and other hedging instruments. In developing these new mechanisms, it is essential that appropriate regulations for financial governance be in place so as to guarantee the rights of savers by enforcing rules on transparency and the timely provision of full, accurate information.

13. Public development banks have an important role to play because they can channel resources into areas in which the volume or terms of the resources offered by the private market are suboptimal, as in the case of financing for both rural and urban micro- and small enterprises, low-cost housing, sustainable development, productive restructuring and technological innovation. In order for this effort to bear fruit, however, there must be maximum transparency regarding the fiscal cost of the subsidies provided through development banks, and every effort must be made to ensure that obligations are met on time, preferably through the use of private institutions as first-tier agents for the channelling of resources.

14. Boosting export capacity is essential in order to achieve an adequate level of external resources and to

* Based on a document entitled "Growth with stability: financing for development in the new international context" (LC/G.2117(CONF.89/3)), presented by the Executive Secretary of ECLAC.

reduce external vulnerability. It is important, therefore, to generate a pro-export environment based on competitive exchange rates, active export promotion policies and the creation of conditions of systemic competitiveness through the development of quality infrastructure and dynamic chains of production. In order for such an effort to be successful it is essential to improve conditions for access to external markets for goods and services.

15. Higher investment and savings rates, financial development and the expansion of exports must be combined, at the national level, with efforts to reduce the extreme vulnerability of the region's economies to external financing cycles. This means, in particular, that booms in financing must be managed on the basis of clearly defined prudential criteria since the seed of economic crisis are sown during periods of excessive capital inflows that gradually undermine the macroeconomic fundamentals of the receiving countries.

16. ECLAC suggests that such situations be dealt with through a combination of general public-revenue stabilization funds; tight monetary and credit policies during booms; prudential regulation of the capital account, preferably through price-based instruments; strong prudential regulation and supervision of financial systems and their active management during booms to forestall the accumulation of excessive risk; and a "liability policy" designed to improve the maturity profiles of public and private debt, both internal and external. In addition, although there is no such thing as a perfect exchange rate regime for every country in every circumstance, the ECLAC document discusses the advantages of a managed flexibility that is designed to reconcile the conflicting demands for stability and flexibility that must be met by today's exchange rate regimes.

17. The external context should provide three essential elements: first, access to markets for our exports; second, a new international financial architecture which, with improved governance, will ensure greater stability for capital flows; and third, mechanisms to ensure that the relatively less developed countries also have access to adequate amounts of external resources on satisfactory terms.

18. The effort to boost exports must go hand in hand with access to external mark ts. The industrialized countries are still applying highly protective policies to agricultural products and "sensitive" manufactured goods from developing countries, and they often display a protectionist bias in applying contingency rules and erecting technical barriers against our exports. In addition, the island countries that have seen a significant erosion of their trade preferences need to receive adequate resources and technical support so that they can modernize and diversify their export base.

19. The tremendous instability of the international financial system is associated with the sharp asymmetry that exists between the world's burgeoning financial markets and the absence of suitable macroeconomic and financial governance at the international level. Better governance can only be achieved through an improved coordination of macroeconomic policies on the part of the major developed countries so as to guarantee greater global macroeconomic stability and the acceptance, on the part of all countries, of mechanisms for ensuring prudential surveillance of macroeconomic policies. International financial stability also depends on the existence of an appropriate global institutional framework that includes minimum standards for prudential regulation and supervision of the financial and information systems that are essential to the proper operation of financial markets. Finally, appropriate institutions are needed to deal with crises.

20. These institutions may be of two types. First, it is important to improve the countries' capacity to offer emergency financing in times of crisis and to develop suitable mechanisms for providing liquidity to countries with strong macroeconomic fundamentals when they are faced with problems of contagion. In both cases, the objective can only be achieved if the International Monetary Fund (IMF) has been supplied with resources of its own through temporary issues of special drawing rights (SDRs). It should be noted, of course, that an increased use of SDRs within the international financial system is an end in itself which has long been advocated by developing countries. In order to avoid problems of moral hazard, however, such special financing mechanisms must be tied to the creation of instruments for permitting private agents to become involved in the solution of crises. Without detriment to the principle of voluntary negotiations between creditors and debtors, international rules must be designed to guarantee the participation of all parties in such negotiations and to prevent them from

continuing indefinitely; this can be done by developing suitable multilateral arbitration mechanisms.

21. Ensuring access to resources entails the development of mechanisms for enabling all the countries to benefit from foreign direct investment and private credit flows. Foreign direct investment is fairly well distributed in the region, although priority attention still needs to be devoted to its linkage with the local economies involved. Private credit flows are much more concentrated, and mechanisms must therefore be developed to provide for guarantees or co-financing by multilateral development banks as a means of facilitating access to the market for countries that have not benefited from these flows. Such efforts are already being undertaken in some new areas of private investment, especially infrastructure.

22. The multilateral banks have made a significant contribution to financing for the region, and they will continue to play a decisive role in the future. First and foremost, they play an essential role in the mobilization of resources for the relatively less developed countries. Their loan portfolios for all the countries of the region are diversified, and reflect the priority these institutions give to social development, sustainable development, state reform and the channelling of resources to micro- and small enterprises, among other activities of high social priority. They also offer better terms, as regards both costs and maturities, than private financial institutions, even in the case of countries in the region that have higher relative incomes; this circumstance indicates that private markets may sometimes overestimate risk, especially — but not only — in times of crisis. Finally, multilateral banks provide financing on a counter-cyclical basis, thereby helping to mitigate external shocks. In particular, they provide the only source of long-term financing that is available during a crisis. This support has been essential even for countries that have higher relative incomes, and it has been decisive in renewing trust in the countries affected.

23. Official development assistance (ODA), for its part, continues to play a key role in providing financing for less developed countries and in providing global public goods or goods with strong externalities, such as peace, sustainable development and the struggle against the worldwide problem of drugs. The main priorities for the future should include the effort to meet the goal, agreed upon within the framework of the United Nations, of supplying 0.7 per cent of the gross domestic product (GDP) of the industrialized countries and the need to ensure that the use of those resources is more transparent and efficient. For its part, the heavily indebted poor countries (HIPC) debt initiative, for which four countries in the region may be eligible, should be made more flexible, and adequate resources should be provided for its financing. This must be done in order to ensure that other developing countries are not required to shoulder a disproportionate share of that financing, either directly or through wider interest-rate spreads and reduced availability of resources for technical cooperation from multilateral banks.

24. In the construction of this global edifice, three requirements must be borne in mind. The first is to ensure the adequate participation of the developing countries in the relevant institutions. The second is to uphold the countries' autonomy in adopting whatever policies they deem appropriate for their development. The third is to ensure that international standards take into account the absorption capacity of the individual countries, given their different levels of institutional development.

25. The decisive role that the region's institutions play in the positive interaction between national efforts and an adequate international context should be stressed. These institutions address a wide range of concerns, including trade integration agreements, which are crucial to the diversification of the export base of our countries; the large network of development banks formed by the Inter-American Development Bank and the subregional development banks, which are the main source of multilateral financing in our region; the Latin American Reserve Fund, a nearly unique institution in the developing world, which has performed so well in the Andean Community over the last few decades and has begun to expand its membership; and recent efforts to coordinate macroeconomic policies. The region must strive to consolidate all these processes and institutions and to deepen regional cooperation as a whole. The development of sound regional institutions does not work against globalization. On the contrary, it contributes to the construction of a much stronger global edifice.

III. Thematic panels

Panel 1. External crisis prevention and management: systemic aspects and national policy

26. The panel members noted that financial globalization affords significant efficiency gains in financing for development, but that it is taking place within an international financial system that has been rendered unstable by the sharp asymmetry existing between the dynamic development of financial markets and the absence of satisfactory macroeconomic and financial governance at the world level. Consequently, it is urgent that major reforms be made in the design of the international financial architecture and in the macroeconomic policies of the countries of the region. In order to attain international financial stability, an appropriate institutional framework is required that includes standards of prudential regulation and supervision. The participating countries emphasized that in order to work towards improving the international financial system, it is important for the developing countries to play a suitable role in the relevant institutions, for there to be an appropriate level of autonomy in national policy-making, and for international rules and standards to take countries' levels of institutional development and absorption capacity into account.

27. From an international perspective, it is important to make certain that the major economies' macroeconomic policies are consistent, to have financial regulations in place that will prevent the build-up of excessive risk, and to see to it that regional, subregional and multilateral agencies, as well as private agents, have a rapid-response capacity in countering threats to stability. The design of that new international financial architecture should ensure the adequate participation of the less developed countries.

28. It is also important to strengthen the International Monetary Fund's capacity to provide exceptional financing during crises, and to develop suitable mechanisms for supplying liquidity to countries with solid macroeconomic fundamentals that are experiencing problems of contagion. The valuable contribution that subregional organizations, such as the Latin American Reserve Fund (LARF), can make in preventing and coping with external liquidity constraints and crisis situations has also been recognized.

29. From a national perspective, progress needs to be made in strengthening financial regulatory and supervisory systems, ensuring a counter-cyclical form of macroeconomic policy management, diversifying exports as a means of reducing external vulnerability, and enhancing governance, which encompasses political, institutional, judicial and social factors as well as economic variables. In addition, financial booms need to be managed prudentially since economic crises incubate during periods marked by excessive capital inflows.

30. There are three courses of action countries can take to protect themselves from external fluctuations: first, the adoption of sound fiscal policies with a structurally balanced focus and an inter-temporal horizon; second, the adoption of sound monetary policies founded upon the existence of an autonomous central bank, whose main task is to keep inflation under control; and third, the adoption of measures to control the open positions taken by banks and their main debtors while avoiding currency and maturity mismatches.

31. The participants in the general discussion noted the importance of the private sector's involvement in solving crises, especially in connection with debt restructuring. Emphasis was also placed on the proposal that IMF create special drawing rights on a temporary basis as a means of building confidence during times of crisis.

Panel 2. Access to external resources for financing development

32. The panellists stressed the importance of having access to external resources on a permanent basis, and noted that the volume, timing and terms and conditions of such financing are often incompatible with countries' needs. All countries should benefit from foreign direct investment (FDI) and private credit flows. FDI is fairly well distributed in the region, but private credit flows are much more concentrated, and systems of guarantees or co-financing mechanisms should be developed by multilateral, regional and subregional banks in order to provide countries that have not benefited from those flows with greater market access. In that connection, they discussed the

idea of a globalization "ethic" oriented towards supporting development efforts to overcome poverty and underemployment and to do away with their migration-related manifestations.

33. They underscored the role of multilateral, regional and subregional institutions in attracting capital to the region, and thereby helping to make up for private investors' lack of interest in projects having a high social rate of return. The panellists also called for steps to ensure a more permanent form of access to financing from multilateral institutions and to strengthen regional and subregional development banks. Regional institutions, for their part, were assisting with the intermediation of financial resources directed towards the region, and their efforts in that respect were oriented by their Latin American identity and their autonomy. They had enhanced their capacity to play a catalytic and counter-cyclical role as financial intermediaries helping to strengthen national financial systems, backstopping macroeconomic management and providing long-term financing for a broad project portfolio aligned with the needs of the countries.

34. In examining countries' renewed access to private financing in the form both of FDI and of equity investment and debt flows, the stability of the former was contrasted with the high degree of variability exhibited by the latter. The panellists recognized the value of FDI flows but also drew attention to their possible effects on external equilibria when profits are repatriated, their concentration in certain sectors and their impact in terms of the creation of enclaves within the region's economies. In view of the foregoing, the panellists called for the consolidation of proactive policies to encourage FDI flows and promote productive development, along with steps to strengthen the production linkages that enhance their economic impact. They also felt that it is necessary to make a greater effort to channel most official development assistance to the countries that are relatively less developed and are the most vulnerable to external shocks.

35. In order to gain access to other private debt and equity investment flows, the practices used in generating financial and accounting information will have to meet international standards. In order to deal with vulnerability and volatility, it was recommended that increases in domestic saving and investment be set as a medium-term goal. With regard to the latter, the importance was underlined of trade liberalization and broad market access since those conditions would make it possible to obtain the foreign exchange needed to fulfil payment obligations.

36. The panellists spoke of the need to establish mechanisms for the regulation and supervision of national financial systems with a view to prudential liability management and to provide support for regional institutions' contingency mechanisms so that they can act swiftly when emergencies arise during crisis situations.

37. In considering new sources of financing for development, the panellists referred to the increasingly important role of the remittances sent back by migrant workers living abroad, noting that such flows occur not only between the region and the more developed economies but also within the region, and that steps could be taken to strengthen mechanisms for channelling those remittances into productive uses.

Panel 3. The decisive role of trade as a factor in financing

38. The panellists stated that exports are extremely important as a source of financing for imports, and that trade in general is a key growth factor. Export capacity must be strengthened in order to secure an adequate level of external resources and reduce countries' external vulnerability. Trade also plays a decisive role in the smaller countries and island States. However, persistently low levels of export diversification continue to act as a source of external vulnerability, with negative implications for stability, investment and growth; a climate conducive to export promotion must be created through moderately high and stable real exchange rates, which would help to avoid an anti-export bias and enhance systemic competitiveness.

39. In terms of active export promotion policies, panellists advocated promoting technological diffusion, given the shift in trade patterns towards intra-industry trade. To that end, trade liberalization should be accompanied by unhindered access to technology in order to avoid asymmetries in market access. At the same time, production and export capacity must be strengthened through the provision of appropriate financing, which is vital for small economies that have seen an erosion of their preferential access arrangements.

40. The panellists and participants in the debate pointed out that the small economies require temporary support to improve their access to external markets and clearly defined rules to protect them. They underlined how necessary it was for those countries to participate alongside the other developing nations in economic decision-making. Due consideration must be accorded to the specific problems and vulnerability of their economies and to the absence of the preferential treatment that should be a founding principle of the multilateral trading system. Under those circumstances, barriers continue to be erected that block those countries from actually sharing in the benefits of globalization. Attention was drawn to the World Trade Organization (WTO) programmes aimed, inter alia, at keeping markets open even during crises. Nevertheless, it was noted that some small countries are at a disadvantage in terms of access to external markets. Consequently, island States are in need of sufficient resources and technical assistance to modernize and diversify their export base.

41. In closing, it was noted that integration processes play a key role since they are conducive to export diversification and would make it possible to increase exports involving a higher degree of processing.

Panel 4. External constraints and the debt overhang

42. The panellists noted that debt, which is one of the most serious problems and greatest obstacles to growth and development, can have enormous political implications that could affect all the countries of the region, regardless of their relative income level. While there are debt relief initiatives for poor countries, there should also be such initiatives for the other countries of the region. In any event, such initiatives should not be regarded as a substitute for other sources of financing, especially in the case of official development assistance. Such assistance should be re-established on the basis of internationally agreed goals and should be channelled to the relatively less developed countries, small island States and countries troubled by armed conflicts or the scourge of illicit drugs.

43. By the same token, moratoriums should not be regarded as a substitute for emergency financing when problems are being experienced in relation to liquidity or solvency. In general, it was recommended that debt reschedulings be undertaken on the basis of universal principles having to do with voluntary agreements among the interested parties, multilateral arbitration mechanisms and IMF financial support.

44. The role of the HIPC debt relief initiative was highlighted, and it was noted that 20 countries have benefited from it in the year 2000. The steps involved in qualifying for that initiative need to be streamlined in a way that will not raise the cost of multilateral credits or undermine international agencies' ability to continue with their lending programmes.

45. With a view to ensuring the success of the HIPC initiative, a number of other observations were made, including the following: it could be coupled with trade agreements; although that initiative was an extremely important form of assistance, it should be viewed as simply one more component in the broader process of obtaining additional resources; the more developed countries should take on more responsibility for its financing; and regional and subregional banks should increase their participation in the initiative, and should modify the eligibility requirements to include relatively higher-income countries.

Panel 5. National aspects of financing for development

46. During the debate, it was noted that both domestic saving and investment have remained low in the countries of the region. The main challenges to be met in order to mobilize national resources are therefore to promote saving and improve financial intermediation. In order to promote saving, a number of political and economic complexities must be taken into consideration, including the need to build confidence in order to pave the way for saving and investment, which requires predictability; and the short-term costs of such an undertaking. A distinction must be drawn between incentives for saving and incentives for ownership. It is also important to encourage self-financing, chiefly through the reinvestment of corporate profits, personal and household saving for specific purposes, and public-sector saving.

47. In order to channel saving into investment financing more efficiently, it is necessary to improve financial supervision and regulation by implementing supervisory mechanisms more effectively and passing more effectual legislation on prudential regulation; to

develop capital markets as a means of achieving greater transparency together with accurate, timely information; and to attain greater governance. Development banks should play an important role in channelling saving into investment.

48. In discussing the necessary conditions for taking fuller advantage of the opportunities offered by globalization, special mention was made of the need to backstop financial development in certain areas that offer high social rates of return but are subject to market failures. Such areas include exports, technological diffusion, the activities of economic agents that were conducive to complementarities, cooperative economies of scale, micro- and small enterprises, and other activities that contribute to social sustainability. Along those same lines, a new domestic financial design was proposed that would include investment funds, risk capital funds and guarantee funds.

49. The panellists analysed the inputs that the region could provide for the High-level Event. They considered the importance of non-financial aspects, one of which is legislation, in attracting capital at a time when saving and investment were declining. Attention was drawn to the progress made by the region in such areas as public finances, banking supervision and regulation, and the development of social insurance systems. In discussing the challenges that remain to be met, mention was made of the fact that little is known about how different types of businesses in the region behaved, how to deepen its capital markets and how to improve financial governance.

50. The development of the financial system is one of the determinants of saving and investment behaviour that were directly and indirectly affected by economic policy. To promote the development of that system, it is important to have macroeconomic stability; clearly defined and staunchly defended property rights; sound accounting procedures; transparency and an absence of corruption; as few barriers as possible to non-traditional banking activities; and an effective safety net.

51. The panellists commented upon the difficulties involved in developing the financial sectors of small economies, and noted that they engage in less intermediation of real saving than of financial saving (which although it influences the level of investment, does not actually determine it). Consequently, such economies must continue to rely on support from multilateral agencies while they gradually upgrade their financial systems as their economic development process progress.

52. The fuller an economy's integration into the international financial system, the more its country-risk premium influences domestic interest rates. Since those premiums stay high even after a crisis has passed, investment remains low. To reduce those risk premiums, it is vital to have support funds, such as the contingent credit lines that have already gained acceptance as a mechanism to be used in crises brought on by contagion. It is also essential to increase the coverage of those lines by broadening the definitions of volatility and contagion. In many countries, borrowing requirements are determined by stock-related difficulties that are reflected in debt service and remittances from FDI, and in some cases a reduction in the public deficit has no influence on borrowing requirements or risk premiums.

IV. Towards the High-level Event: the perspective of Latin America and the Caribbean

53. As part of the work of the Regional Consultation, a group open to all delegations from the Latin American and Caribbean countries was formed which worked concurrently to consider the views of these member countries of the Commission. The group approved a statement entitled, "Towards the High-level International Intergovernmental Event on Financing for Development", which is set out below.

"Towards the High-level International Intergovernmental Event on Financing for Development

"We, the representatives of the Latin America and Caribbean countries, meeting in the city of Bogotá on 9 and 10 November 2000 for the Regional Consultation on Financing for Development for the Latin America and the Caribbean Region, have adopted the following contribution to the High-level International Intergovernmental Event on Financing for Development, as well as to the substantive preparatory process, as provided for by the

General Assembly in its resolution 54/196 of 22 December 1999.

"Political considerations

"1. In the Millennium Declaration (General Assembly resolution 55/2), our heads of State and Government voiced our concern about the obstacles facing developing countries in mobilizing the resources needed to finance their sustained development, and made the commitment to make every effort to ensure the success of the High-level International Intergovernmental Event on Financing for Development.

"2. A clear consensus emerged: the benefits of globalization must be equitably distributed so as to contribute to eradicating poverty and promote economic and social equity within and between countries. We need to confront the challenges of globalization from a human perspective: international finance for development plays an essential role in the promotion of sustained economic growth and comprehensive social development, and in the prevention of social instability and exclusion of countries.

"3. In the best tradition of the major conferences and summits of the United Nations, it is high time to face the challenges of development at the global scale from the perspective of finance. It is high time to join forces to build a new global consensus with the objective of ensuring that the international economic system functions in a more just and equitable manner, and guaranteeing the security of all peoples and the opportunity to raise their living standards.

"4. The United Nations, in fulfilling its role in the promotion of development, plays an important role in international efforts to build up the necessary consensus for the reforms needed for a more equitable, participatory, solid and stable international financial and trade system, within a convergence of efforts with the Bretton Woods institutions, the World Trade Organization, the regional institutions and a large number of other relevant actors at all levels and sectors.

"5. To this end, it is essential that the process of reform for a strengthened and stable international financial architecture should be based on broadened and strengthened participation of developing countries in the international economic decision-making and norm-setting processes in order to promote more efficient international financial institutions and arrangements in which all relevant interests can be effectively represented.

"6. An important challenge is to renew national, regional and international efforts to promote international financial stability, and to this end to improve early warning, prevention and response capabilities for dealing with the emergence and spread of financial crises in a timely manner, taking a comprehensive and long-term perspective while remaining responsive to the challenges of development within a framework that upholds national development policies and priorities.

"7. Of critical importance is a fair, equitable and rules-based multilateral trading system, operating in a non-discriminatory, inclusive and transparent manner that provides benefits for all countries, especially developing countries. This must involve, inter alia, effective participation of the latter in decision-making, improved market access for goods and services of particular interest to developing countries, and effective and full implementation of special and differential treatment.

"8. The High-level Event should further consolidate a broad agenda in order to address national, international and systemic issues relating to financing for development in a holistic manner in the context of globalization and interdependence. This global agenda should be action-oriented, raising international cooperation for development to a higher political platform.

"9. Bearing in mind the concerns included in paragraph 12, it should address, on a comprehensive basis, the interrelated issues involved in mobilizing financial resources for development in order to, inter alia: (a) make foreign direct investment and other private flows for development more participatory, especially for those countries that are currently marginalized from their benefits; (b) enhance the role of trade in financing for development, guaranteeing the

full participation of all developing countries in international trade and access to international markets for their exports without discrimination of any sort whatsoever; (c) increase international financial cooperation for development through the reactivation of the levels of official development assistance and the fulfilment of the commitment to provide 0.7 per cent of gross domestic product; and (d) meet the challenge of finding an enduring solution for the external debt problem. It should also address systemic issues and seek to increase the coherence and consistency of international financial and trading systems in order to support development.

"10. The High-level Event will give the international community an historic opportunity to jointly create a new world partnership for development, with emphasis on the promotion of economic and social equity on a global scale, while responding to the specific needs of vulnerable countries and social groups.

"Concerns regarding financing for development

"11. Despite the many difficulties faced by our countries, during the past decade they have worked to achieve economic growth with equity. These efforts have been reflected, inter alia, in advances in the areas of macroeconomic management, consolidation of the fiscal situation, economic and trade liberalization, price stabilization, the reactivation and intensification of regional economic integration, and the expansion of South-South cooperation.

"12. Nonetheless, we have major concerns regarding financing for development in Latin America and the Caribbean which should be taken into consideration in the creation of a supportive international environment that will complement our domestic efforts. Some of those concerns are the following:

(a) The vulnerability of our economies to the instability of sources of external financing;

(b) Unequal foreign direct investment and unequal access to private capital markets;

(c) The difficulty of gaining access to resources for conducting many activities with a high rate of return in terms of social investment and sustainable development;

(d) The terms and conditionality imposed on such access, as well as on international funding sources;

(e) The need to strengthen the financing provided by multilateral banks for development;

(f) The limited capacity of the International Monetary Fund and development banks to provide liquidity for purposes of crisis prevention and resolution;

(g) The obstacles to the allocation of resources for development created by the existence of internal conflicts;

(h) The limitations on development imposed by the high level of indebtedness of some medium- and low-income countries of the region;

(i) The difficulties involved in implementing the heavily indebted poor countries debt relief initiative, within a framework of differentiated co-responsibility, while taking into consideration equitable burden-sharing;

(j) The insufficient levels of official development assistance available to countries in need of it;

(k) Current limitations in access to regional and international markets for exports of goods and services of interest to the region;

(l) The need to strengthen the United Nations in fulfilling its mandate in development and to address its marginalization in economic decision-making;

(m) The needs to address asymmetries among countries in trade matters through, inter alia, the effective implementation of special and differential treatment and the fulfilment of commitments; eliminate trade barriers limiting developing countries' access to industrialized countries' markets; and incorporate developing countries' priorities in multilateral trade negotiations and assuring their full participation in the decision-making process;

(n) The lack of progress in the completion of a vulnerability index;

(o) The problems posed by the erosion of trade preferences, supply-side constraints and diversification efforts of small economies and small island developing States.

"Final points

"13. We welcome the document prepared by the Economic Commission for Latin America and the Caribbean (LC/G.2117(CONF.89/3)) entitled, 'Growth with stability: financing for development in the new international context', and we take note of its recommendations.

"14. We express our deep appreciation and gratitude to the Economic Commission for Latin America and the Caribbean, the Inter-American Development Bank and the United Nations Conference on Trade and Development for their contribution to this Regional Consultation.

"15. We also commend the Government of Colombia for its contribution and for hosting this meeting, and we undertake to ensure that this contribution shall be taken into due consideration as an input of Latin America and the Caribbean to the High-level Event, and its substantive preparatory process."

V. Other contributions to the debate

54. Two delegations requested that their statements be included in the report. Their statements are accordingly reproduced below.

Statement by the representative of Saint Lucia on behalf of the countries of the Caribbean Community

"The Caribbean States would like to thank the Government of Colombia for graciously hosting the Regional Consultation on Financing for Development for the Latin America and the Caribbean Region.

"We are extremely pleased to be participating in this process, which we believe is long overdue. We believe too that financing for development should have been the first international conference to be convened since it is the foundation upon which a development agenda is both built and financed. This is the critical missing link in the development agenda, without which implementation of a development agenda cannot proceed.

"We are happy, therefore, that although it is being done in reverse order, financing for development is being discussed at the global level at the turn of the century.

"Financing development is an issue of significant importance to small States, in particular the small economies and the small island developing States of the Caribbean, which face enormous challenges in financing their development given their inherent weaknesses and vulnerabilities and the hostile globalizing economy.

"While we recognize that there are six agenda items, we will address mainly trade, systemic issues and an international enabling environment.

"In relative magnitude, global financial flows are much greater than trade flows; however, for most developing countries, the loss of revenues due to trade restrictions is much larger than their external financial sources, so that in terms of relative importance, opening developed country markets to import more goods produced by developing countries generates more inflow than external financing.

"Opening markets, however, is not all. Export capacity and access to technology are preconditions to benefiting from increased market access, which is important since the resources generated by trade must be converted into foreign imports. The evolution of technology has been such that the manufactured goods that are produced by developing countries who have diversified their exports baskets tend to behave exactly as primary products, with falling prices and thus declining terms of trade relative to developed country manufactured goods.

"The global economy is supported by three major pillars — financial, monetary and trade — and three main institutions — the World Bank, IMF and WTO — exercise special responsibilities in these areas.

"The thrust of the General Agreement on Tariffs and Trade (GATT) and WTO remains

trade liberalization to achieve economic growth, yet the records show that liberalization has occurred mainly in developing markets, and those areas of interest to developing countries where they have a competitive advantage remain protected in developed markets. In fact, it is estimated that $100 billion will be gained by developing countries to finance their development if developed countries cut their trade barriers by 50 per cent.

"1997 figures reveal that the Organisation for Economic Cooperation and Development (OECD) countries with 9 per cent of the world's population or about one billion of the six billion of us on earth, have 86 per cent of the shares of world gross domestic product (GDP), 82 per cent of world export markets, 68 per cent of FDI and 91 per cent of all Internet users, with 80 per cent of web sites operating in English.

"Over 60 per cent of the world's population, or about five billion of us in the developing world in about 160 countries, share only 13 per cent of the world's GDP, 17 per cent of world trade and 6.5 per cent of Internet use and income and poverty gaps continue to widen between developed and developing countries.

"When the architects of the global economy formulated policies and institutions after World War II to globalize the economy, it was with the hope of attaining full employment, financial stability, more equitable distribution of income and benefits of free trade, but by playing by the rules of the international financial and trading systems. This system of rules set by developed countries is still being applied by developed countries, ignoring the different strengths and stages of development of developing countries and varying natural endowments. It has continued to ignore, for 50 years now, the glaring disparities and inequities of the current trading system.

"It must be noted that developed countries have only partially liberalized their markets and did so only after they had developed the necessary infrastructure and stages of development to liberalize. Even then, special provision was made for the disadvantaged and weak economies — a Marshall Plan to assist them in developing and integrating into the global economy.

"Yet, special and differential treatment to assist developing countries in bridging the disparity gaps and addressing differences remains largely unimplemented and has no legally binding status. There is still no recognition of the limitations, inherent vulnerabilities and structural weaknesses of the small and vulnerable, who are seriously marginalized in the rapidly globalizing economy.

"Trade is still one of the major contributors of finance for development to many developing countries, including small States in the Caribbean. In fact, a structural disadvantage for us is our narrow economic base, with heavy dependence in trade in one commodity, which provides over 50 per cent of current export earnings in the case of Saint Lucia. The incomes of small developing States are 25 per cent more volatile than those of our larger counterparts, and the citizens of small countries have less capacity to insure domestically against adverse shocks to income. A current case is the liberalization of the one agricultural commodity through the erosion of trade preferences given as development assistance to disadvantaged economies. The low diversification in production and trade and susceptibility to natural disasters explain much of small States' income volatility. In fact, Saint Lucia has lost about 50 per cent of its revenues in export earnings to liberalization in the agricultural sector. The same holds true for other Caribbean countries.

"Vulnerability to natural disasters and external shocks, our small markets and narrow economic basis are but part of the challenges faced by small economies. Others include high energy and transportation costs, and weak human and institutional capacities in both the public and private sectors, complicated by scattered populations. The sum of all which is a high development cost for small economies.

"The Caribbean States are attempting to diversify but are in need of reasonable periods of transition and adequate financing. Already, diversification efforts are seriously challenged by OECD in the financial services sector.

"We are therefore asking that the special and serious concerns of the smaller members of the Latin America and Caribbean region be adequately addressed in the action section of the outcome document of the Regional Consultation, in particular special effort to offset terms of trade losses.

"In the wider context of the financing for development process, there are other important elements that CARICOM wishes to see reflected in the action section report of the consultation.

"Earlier reference was made to the glaring inequities of the global economy, which to a large extent are due to systemic and structural imbalances in the global economic system, in particular the undemocratic decision-making processes of the monetary, financial and trading institutions. Hence our call for reform and effective participation of developing countries. We would also like to see promoted a central role for the United Nations — the only legitimate international institution mandated to ensure equity in the distribution of benefits of the global economy. In this regard, the role of the United Nations in policy coherence and coordination must be strengthened.

"Another important contributor to financing development in developing countries is ODA. The United Nations has an agreed target of 0.7 per cent of GDP in assistance to developing countries. The difference between the agreed 0.7 per cent and the delivered 0.24 per cent is over $100 billion that are denied developing countries annually in their development efforts.

"Yet developed economies are the strongest they have ever been and the decline in ODA continues. This denial of development assistance must be strongly reflected in the outcome of the Regional Consultation.

"The crippling debt of developing countries is another major obstacle diverting urgently needed finance for development from developing countries to developed countries. The cancellation of debt would make available $2,554 billion in financing for the development of developing countries. A strong call needs to be made for the cancellation of the debt of poor to give them a chance to develop and benefit from the global economy.

"The financing for development process is a very critical one for developing countries. It is our last opportunity in this millennium to claim the promise of free trade for our poor people and underdeveloped economies. It will be the only chance in the beginning of the new millennium to ensure equity in the sharing of the benefits of the global economy and peace security and development for our people."

Statement by the representative of the United States of America

"The United States expresses its appreciation to the Government of Colombia for hosting this consultation, and would like to thank the Economic Commission for Latin America and the Caribbean for organizing the meeting.

"We find this regional meeting timely and necessary at this juncture of the preparatory work on financing for development. We welcome the participation of the Finance Ministers of many Latin American countries, and encourage their continued participation in the preparatory process and in the final event.

"We welcome the emphasis made during the conference by many Latin American countries' Finance Ministers on the importance of sound economic and social policies, trade liberalization, good governance, the rule of law and democratization.

"Experience demonstrates that there are no alternatives to sound policies if there is to be sustainable progress on economic and social development.

"In addition, we appreciate the work done by the Government of Colombia on the 'Bogotá Declaration', and recommend for ECLAC consideration, in particular, the following national policy recommendations from the 'Declaration' as important actions to address some of the key development financing questions facing the region:

- Maintenance of stable and transparent ground rules that will uphold the rights of owners of financial and production assets in the face of the

discretionary powers or actions of public and private third-party interests;

- Consolidation and/or intensification of fiscal adjustment policies through, inter alia, increased productivity of public expenditure, stronger tax systems, the introduction of public revenue stabilization funds, greater transparency in fiscal accounts, and suitable means of estimating and financing the explicit and implicit guarantees granted by the State;
- Establishment or consolidation of proactive policies that favour foreign direct investment and other long-term capital flows;
- Securing the solvency of the banking system, the prevention of systemic risks, and the sound management of credit risk, terms and currency;
- Upgrading the practices employed for the compilation of financial and accounting information according to international standards.

"We believe these recommendations are a valuable contribution to the financing for development exercise. We urge the Preparatory Committee for the High-level Event to take them into account in its preparatory work to shape the agenda for the final event.

"The United States believes that the 'preliminary agenda' for the final event should be further distilled to reflect international consensus. We urge the Preparatory Committee to focus the final event on the following issues, on which wide agreement exists among member States:

- Mobilizing domestic financial resources for development — macroeconomic policy formulation and implementation and private financial sector development;
- The importance of transparency, governance and the rule of law for mobilizing international resources for development — private capital flows, foreign direct investment, ODA and debt relief;
- The importance of using development resources effectively, with particular attention to promoting private enterprise and basic social services;
- Trade — global, regional and country-level trade liberalization and cooperation, and trade-related capacity building for trade-led growth.

"The Preparatory Committee should strive to avoid highly controversial issues that could potentially derail the final event. For example, we are concerned over the insistence on a substantive role for the United Nations in the work of the international financial institutions (IFIs). Attempts to impose United Nations prescriptions on the IFIs is interference in their organizational and decision-making autonomy; it is also counterproductive, especially at a time when the IFIs' input is most needed to ensure the success of the financing for development exercise.

"In this regard, we want to emphasize the importance of the United Nations consulting fully with the World Bank, IMF, and, if appropriate, WTO, in shaping the financing for development agenda, to ensure that these institutions feel comfortable with it and can provide useful substantive input."

Annex

List of panellists

Panel 1
External crisis prevention and management: systemic aspects and national policy

Presenter:

José Antonio Ocampo, Executive Secretary of ECLAC

Panellists:

Juan Manuel Santos, Minister of Finance and Public Credit of Colombia

Nicolás Eyzaguirre, Minister of Finance of Chile

Antonio Gustavo Rodrigues, Deputy Secretary for International Affairs of the Ministry of Finance of Brazil

Roberto Guarnieri, Executive President of the Latin American Reserve Fund

Reinhard Munzberg, Special Representative of the International Monetary Fund to the United Nations

Federico Rengifo, Deputy Minister of Finance and Public Credit of Colombia

Panel 2
Access to external resources for financing development

Presenter:

Andras Uthoff, Coordinator of the Special Studies Unit of the Office of the Executive Secretary of ECLAC

Panellists:

Leonel Baruch Goldberg, Minister of Finance of Costa Rica

Manuel Fragoso Diez, Assistant Director for Finance for South America, Ministry of Finance and Public Credit of Mexico

Luis Enrique Berrizbeitia, Vice President of the Andean Development Corporation

Jan Kregel, Senior Advisor of the United Nations Conference on Trade and Development

Eduardo Fernández Arias, Lead Research Economist, Inter-American Development Bank

Jairo Montoya, Deputy Minister for Foreign Affairs of Colombia

Panel 3
The decisive role of trade as a factor in financing

Presenter:

Reinaldo Bajraj, Deputy Executive Secretary of ECLAC

Panellists:

Alister McIntyre, Chief Technical Adviser of the Caribbean Regional Negotiation Machinery of the Caribbean Community

Clemens Boonekamp, Director, Trade Policies Review, World Trade Organization (WTO)

Jan Kregel, Senior Adviser of the United Nations Conference on Trade and Development

Panel 4
External constraints and the debt overhang

Presenter:

José Antonio Ocampo, Executive Secretary of ECLAC

Panellists:

Marcos Carias, Adviser on external debt, Ministry of Finance of Honduras

Ewart Williams, Senior Adviser, Western Hemisphere, International Monetary Fund

Alister McIntyre, Chief Technical Adviser of the Caribbean Regional Negotiation Machinery of the Caribbean Community

Panel 5
National aspects of financing for development

Presenter:

Manuel Marfán, Expert on economic development, Office of the Executive Secretary of ECLAC

Panellists:

Maria Cecilia Otoya, President, Industrial Development Institute of Colombia

Gert Rosenthal, Permanent Representative of Guatemala to the United Nations

Guillermo Perry, Chief Economist for Latin America and the Caribbean of the World Bank

Courtney Blackman, Expert on Central Banking Systems in Developing Countries and former President of the Central Bank of Barbados

Roberto Frenkel, Director, Banco de la Provincia de Buenos Aires, Argentina

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Second substantive session
12-23 February 2001

Financing for development: hearings with civil society, 6 and 7 November 2000

Summary of panel presentations and discussion

Summary

In its resolution 54/279, the General Assembly decided that the Preparatory Committee for the High-level International Intergovernmental Event on Financing for Development would hold two sets of hearings with civil society organizations and the business community to consider their views on areas of the financing for development agenda.

The civil society hearings were held in New York on 6 and 7 November 2000, and the present document summarizes the presentations made by 23 panellists, representing civil society organizations. It provides a synopsis of the dialogue among delegations, panellists and other NGO representatives that took place during the hearings.

The main areas of discussion were:

(a) Mobilizing domestic financial resources for development (sect. I);

(b) Mobilizing international resources for development: foreign direct investment and other private flows; and trade (sect. II);

(c) Increasing international financial cooperation for development through, inter alia, official development assistance; and debt (sect. III);

(d) Addressing systemic issues: enhancing the coherence and consistency of the international monetary, financial and trading systems in support of development.

The statements made at the hearings are available on the Internet at:

http://www.un.org/esa/ffd/hear_panel_list1.htm

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I. Mobilizing domestic financial resources for development

Moderator:

Asda Jayanama (Thailand), Co-Chair of the Preparatory Committee

Panellists:

Fernanda Carvalho, Brazilian Institute of Social and Economic Analyses

Bart Bode, Head of Policy Department, Broedelijk Delen; member, International Cooperation for Development and Solidarity

Julian Disney, President, International Council for Social Welfare

Roberto Rubio, Director, International Foundation for Development; Coordinator, Structural Adjustment Participatory Review International Network — Latin America

Filomeno Santa Ana, Director, Action for Economic Reforms; Economist, School of Economics, University of the Philippines

Zo Randriamaro, Programme Manager, Gender and Economic Reform in Africa, Third World Network Africa

Social development and poverty alleviation

1. Ms. Carvalho outlined four key expectations of the financing for development process. First, it should assist national and international financing systems in becoming actively supportive of social equity and people's welfare. Second, the process should encourage transparency. It should bring issues of financial policy and decision-making, which are usually the opaque province of finance ministers, bankers and the international financial institutions (IFIs), into the open, engaging those parties to respond to the interests of wider social groups. Third, it should stimulate exchanges of experience in applying different fiscal policy measures for meeting people's needs. Finally, the process should recognize the diversity of developing countries by focusing on different regional experiences.

2. In making these points, Ms. Carvalho suggested that:

(a) The distinction between domestic and international resource mobilization may now be obsolete. It may be more useful to distinguish between countries that have access to private capital and those that do not;

(b) Markets are extremely important to the first group of countries, but pure market forces can punish progressive social policies. Negative developments, such as capital flight and crony capitalism, can weaken national currencies and cause wide social damage, while national measures to address social contract issues, such as labour rights, can become deterrents to foreign investment;

(c) The goal of the financing for development process must therefore be to define a role for the state that is not in opposition to market-generated growth but which helps to correct distortions created by markets in order to achieve patterns of quality growth compatible with social values.

Financial speculation and domestic tax systems

3. Mr. Bode of International Cooperation for Development and Solidarity (CIDSE) elaborated his proposal for a domestic currency transaction tax. The new proposal moves beyond the original ideas expounded by James Tobin in 1972 and is based on a dual taxation system: first, a minimum tax set at a very low level (0.01-0.02 per cent) to provide constant income and facilitate the transparent monitoring of currency flows during normal market development, and second, a ramped-up tax (50-100 per cent), applied as a circuit breaker during a financial crisis.

4. Mr. Bode stressed that the new tax should be a domestic instrument. As such, its introduction would not require an international institution with the power to levy, collect and distribute global taxes. There are precedents for such national instruments. Before the 1997 financial crisis, Chile showed that it is possible to levy the equivalent of a domestic tax on short-term capital inflows to discourage speculation, and after the crises Malaysia acted to restrict local currency movements. It would also be feasible to implement a currency transaction tax. Studies indicated that it would be possible to apply such a tax on the basis of inter-bank electronic networks in place and the daily settlement procedures between national banks.

5. Other arguments for the tax proposed by Mr. Bode included: (a) its role as a tool for prudential

regulation; (b) the protection it would offer small economies against speculative attacks on their national currency, thereby also releasing "immobile" national bank reserves for investment in domestic social development; and (c) its ethical impact as a tax on capital in countering the Western practice of taxing labour disproportionately. Lastly, since money markets are concentrated in a few industrialized countries, the latter would receive substantial extra revenue, which could be allocated for their own domestic purposes and to reinvigorate official development assistance (ODA).

Stronger international standards and cooperation in taxation policy and administration

6. Mr. Disney explained how the International Council on Social Welfare (ICSW) had developed an anti-poverty pact, incorporating the seven international development targets to be achieved by 2015 and initial resource commitments for implementation by 2005. These commitments reflect a mix of domestic and international as well as public and private resources. Most commitments, however, cannot be achieved without international cooperation to adopt significant national tax reforms.

7. According to ICSW, certain basic deficiencies in tax administration, compounded by the effects of globalization, stand in the way of mobilizing significant levels of domestic resources. The main weaknesses include lack of information, resources and political will to administer taxes effectively; promotion of excessive financial and property speculation; encouragement of capital flight; excessive reduction of corporate tax obligations; evasion of tax liabilities by multinationals; increased reliance on inequitable taxes; excessive secrecy provisions; tax privileges that promote unfair trade; and inadequate action to reduce harmful tax competition.

8. ICSW proposed a package of measures to address these challenges, including stronger international obligations to provide information to and between tax authorities; improved international technical and financial assistance for developing country tax authorities; stronger international taxation standards; international adoption of refundable withholding taxes on cross-border payments; international coordination of taxes on multinational companies; a currency transaction tax, as proposed by CIDSE; removal of tax exemptions on e-commerce; the development of an international convention for repatriation of misappropriated funds; and substantial and firm commitments to provide improved ODA and debt cancellation.

9. ICSW also proposed a number of implementation processes: setting up regional expert and technical negotiating units; strengthening the international coordinating role of the Economic and Social Council in tax reform; development through the Council of an international code of corporate conduct relating to tax compliance; and establishment of an international tax forum under United Nations auspices.

Mobilizing internal resources for the national development plan

10. Mr. Rubio stressed that, in mobilizing domestic resources, the key question is: how should such resources be used? While sources of domestic financing are few (usually internal savings and taxes), the possible uses of funds are many. What priorities countries plan to finance and how they finance those priorities are as important as where they obtain the requisite funding.

11. Explaining how El Salvador had developed its national plan, he underscored the role of institutional innovation and social inclusion in transforming budgetary processes into quality national investments consistent with human development goals, the preservation of ecosystems and the basic needs of the poor and excluded. The plan was formulated over two years under the direction of an independent and plural commission. The methodology emphasizes broad participation by all political groups and by all social segments, including the churches. The plan takes a differentiated approach to various regions of the country: in the Gulf region, the focus is on building a world gateway for trade, the South is defined as an exporting area and the North was dedicated to eco-farming. Through this concerted process, plan priorities and financing requirements were finalized on the basis of a genuine national consensus around the needs of different segments of society.

12. Sources of funding were tackled through a series of changes. It was decided to increase the 10 per cent general tax rate, change the distribution system by redressing imbalances between direct and indirect taxes through a new tax pact, reform the private banking system, reorganize the social security system to reflect

workers' interests and emphasize local counterpart funds for development schemes. Measures to stimulate savings and reinvest business profits in long-term growth were also adopted.

Mobilizing and retaining domestic financial resources in Africa to support local production in strategic sectors which affect women

13. Ms. Randriamaro presented a comprehensive case that liberalization has combined with the peculiar characteristics of African economies to put women working in strategic economic areas, notably agriculture and the food sub-sector, under even greater financial pressure. The situation calls for alternative policy responses.

14. Ms. Randriamaro observed that, in Africa, subsistence and commercial activities very largely involve small and microenterprises, many of which are organized by women and sustained by women's labour. These enterprises normally face acute financing gaps because: (a) financial instruments, such as credit, insurance and banking, are skewed in favour of import-export trade and cash crop sectors, and (b) weak, open African economies that are excessively vulnerable to external factors experience disproportionate outflows of resources. Before liberalization, these gaps were partly compensated for by targeted financial support through specialist agricultural banks. However, with the move to free market policies and the liberalization of financial services, such support has been abandoned. The general policy framework encouraged by the IFIs has become inimical to sectors key to sustainable growth and national development. Moreover, the financing vacuum in agriculture has not been filled by the private sector. Ms. Randriamaro pointed out that a major consequence of these macro-factors was that women, far from benefiting from market-led financial sector reforms, have found themselves trapped in a "microfinance ghetto". Studies indicated that microfinance might have been overemphasized in conventional approaches to the economic empowerment of women. Such approaches imply that women's productive capabilities should be confined to small-scale or informal activities, when in fact women's demand for services from mainstream financial markets is on the increase and is potentially a major spur to domestic investment and growth. Governments should therefore work with their aid partners to revive and broaden mainstream public financing and credit. This implies a new, more active policy role for Governments, which should re-engage with the national economy. Their new goal should be to devise innovative and supportive institutional frameworks for closing financing gaps in under-served strategic sectors, and for mobilizing the full productive and investment potential of African women.

Progressive tax reform agendas at the national level

15. Mr. Santa Ana emphasized that global rules are an essential support for effective national tax programmes. It is a basic principle that Governments should find the bulk of development financing from their own resources through equitable, buoyant and efficient tax systems. But external pressure to lower tax and tariff rates (fiscal degradation) makes national revenue generation very difficult. Wide differences in national tax systems are encouraging the transfer of resources away from countries, with progressive tax structures towards tax havens and countries using taxes as incentives. Global rules are therefore necessary to achieve coordination and harmonization, address tax evasion problems at the international level, prevent locational competition from becoming a race to the bottom, and help countries to exercise flexibility and autonomy under the homogenizing effects of globalization.

16. Mr. Santa Ana outlined several necessary features of a progressive national tax system, addressing direct and indirect taxes and loopholes leading to tax evasion. He suggested that the private sector be encouraged to participate in financing development in areas where profit and social benefit coincide. However, he cautioned that Governments should not rely on privatization simply to raise revenues. Privatization should proceed on the basis of its specific merits.

Highlights of discussion

Currency transaction tax

17. This proposal provoked four major questions. First, the global trend towards deregulation is a move away from widespread government failure. However, the currency transaction tax is a return to bureaucratic intervention by Governments.

18. How would this proposal address the major issue of government failure? Is the proposal as presented not

too rigid and insensitive to market realities? Second is the question of administrative feasibility. How would financial authorities set about keeping track of manifold global transactions that take place around the clock? It should be noted that both Chile and Malaysia only resorted to such dampening measures for a short period on an emergency basis. Third, implementation of such a measure by one or two countries alone would place them at a competitive disadvantage. Implementation would therefore have to be universal. Is it feasible to expect that all countries would simultaneously enact and enforce this kind of legislation? Finally, it is important to distinguish between the financing of ODA and market services since there are key differences in their respective roles.

19. On the first question, it was observed that markets are larger than Governments and that the consequences of market failure, as in the Asian crisis, might therefore merit greater public attention. In replying to the questions, Mr. Bode noted that the CIDSE proposal entailed a degree of reregulation but that a degree of prudential public regulation was in everyone's best interest. The dual structure of the proposed tax is designed not to disturb the normal functioning of the market but to provide a resort in emergencies. Deregulated markets operate under opaque conditions that offer virtually no scope for justifiable public intervention, such as when market failures cause heavy social crises. The tax proposal tries to address that contingency. Its feasibility has been assessed and upheld through studies such as that by Rodney Schmidt. The functioning of the tax rests on the daily final settlement process at the National Bank, which provides a 24-hour check on all currency movements. Universal implementation poses a challenge that will require some form of international coordination.

Role of the private sector and other sources of financing

20. It was asked how, in addition to broadening and deepening the tax base, countries should directly stimulate other sources of creative energy for financing development. What do NGOs believe should be done to create an enabling environment for private sector contributions? What role could be played by large pension funds, which account for substantial resources? In response, Mr. Santa Ana spoke about public-private roles. The private sector should focus its energies and resources on responsible growth objectives possibly in urban environments. This would free the state to target major anti-poverty measures in other areas. On the role of pension funds, he observed that there is an inherent conflict between the profit maximization motives of fund managers on behalf of their clients and public investment objectives with low financial returns. For pension funds to make a contribution commensurate with their asset base, nations would need to devise rules for using such funds transparently in the public interest. CIDSE agreed that prudential public regulation holds the key to the productive mobilization of private sector resources. One participant noted that, under the 1980s adjustment programmes, many developing countries took external advice and privatized without lasting benefits for their poor. Does privatization offer a durable long-term solution?

National spending priorities and capacity-building for domestic capital markets

21. The Panel was asked to comment on: (a) the statement that government spending priorities should be examined closely; and (b) whether the development of well-functioning domestic stock markets offers new sources of finance. Mr. Disney agreed that national spending priorities are key. A central part of the anti-poverty pact proposed by ICSW relates to reducing military expenditure and sources of leakage, such as corruption. These actions are part of a balanced, two-way pact between Governments and society. On domestic market capacity, there is a lot to be done, including removing distortions encouraging short-term speculation and fixing capital flight by addressing such matters as external tax incentives.

22. It was suggested from the floor that it is possible to over-emphasize the role of taxes in domestic resource mobilization, considering that a broader tax base would affect the informal sector and fledgling entrepreneurs that need incentives. Fixing volatile exchange rates that attack national currencies and addressing corruption, which siphons away large sums of public money, are higher priorities. Mr. Disney replied that the ICSW anti-poverty pact deals with all these issues as a comprehensive package. Fixing exchange rates and addressing corruption have clear external dimensions, including, in the case of misappropriated capital, the issue of the withdrawal by certain countries of withholding taxes on cross-border payments. This panel session, however, looked

primarily at domestic measures, although it is obvious that many national measures are bound up with the external environment.

23. Mr. Rubio agreed that the search for domestic resources is multifaceted and that taxes, although often the primary source, are not the only sources. Pension funds, social security systems and the reinvestment of business profits should be taken into account when trying to broaden and deepen the resource base. It is important to create the political and institutional space for both public and private sources of financing.

Effective intermediary structures for local development

24. Ms. Randriamaro's account of women trapped in a "microfinance ghetto" attracted a number of supportive comments. There is apparently some conflict between macrolevel liberalization policies and microlevel development needs. Microfinance services, while useful as safety nets, might not provide a developmental answer to the question of how to channel financing effectively to enable communities, chiefly women, to prosper in their local context or make their full contribution to economic development. The state evidently has a role to play in providing an intermediary structure between world capital and village-level finance. The representative of Financing for Development Cooperative of Australia suggests that the biases of domestic power structures have more to do with blocking gender equity than rural or microfinancing initiatives themselves. Affirmative political action is required to integrate women with the larger economic system. Accessible, convenient savings systems for poor communities are also required.

25. Ms. Randriamaro was asked to comment further on policy alternatives. She noted that Governments have for too long been content to leave microfinance programmes in the hands of NGOs. These programmes thus often reflect the constraints of NGOs in terms of lending volume and sustainability. High interest rates of sometimes 20 per cent or more are another issue. Instead of attempting to recoup the risk and transaction costs of short-term loans entirely through interest rates that penalize women, it would be better, as the United States Agency for International Development and other agencies have shown, to try and spread the costs of providing microfinance differently. An alternative policy response should start by lowering interest rates and asking Governments to put back effective intermediary financing institutions. Effective community savings schemes should be a part of that response.

Proposals of other NGOs

26. The representative of the International Union for Land Value Taxation drew attention to the benefits of its proposal to shift tax burdens away from labour and productive capital onto land and natural resources. The representative of the Global People's Network reminded participants that the action plans of the 1990s global conferences considered other forms of innovative taxation, such as green taxes, levies on airline travel and use of the electromagnetic spectrum.

27. Nothing has come of these ideas, and it is evident that key development goals in health, sanitation and education have still not been adequately funded. It is time to be serious about the global action plans and commission an in-depth study of these various revenue-generating proposals, including the proposed currency transaction tax. On broadening the tax base, the representatives of ICSW and CIDSE noted that such assets as land are often substantially under-taxed, and that the burden invariably falls on income and labour. This is a question that could be addressed through the international tax forum proposed by ICSW.

28. On necessary funding for the action plans, the representative of CIDSE cited the estimate provided by the *UNDP Poverty Report* of $40 billion annually. The amounts needed are known, and such proposals as the proposed currency transaction tax could raise such sums. The representative of ICSW remarked that its anti-poverty pact is designed to lend new momentum to conference goals, and represent a complete spending and taxing package. The time is ripe for developing countries to leverage the financing for development process to gain a comprehensive agreement on their behalf, including on such matters as ODA and debt.

Corruption

29. The large capital and revenue outflows caused by corruption were commented on by several speakers. It was underlined that there is also a supply side to the issue, including the role played by "rogue corporations" that offer bribes and other inducements to Governments. The proposed international convention for repatriating misappropriated funds

should have some scope to address both public and private corruption.

II. Mobilizing international resources for development: foreign direct investment and other private flows; and trade

Moderator:

Jørgen Bøjer (Denmark), Co-Chair of the Preparatory Committee

Panellists:

Professor Tariq Banuri, Senior Research Director, Stockholm Environment Institute, representing Regional and International networking group of organizations working for sustainable development (RING)

Mariama Williams, Visiting Researcher, Center of Concern, representing the International Network for Gender and Trade, Development Alternatives With Women for a New Era (DAWN) and DAWN Caribbean International

Marina Ponti, Policy Adviser for External Relations, Mani Tese

Yash Tandon, Director, International South Group Network Zimbabwe

Alternative sources of financing: microcredit for sustainable livelihoods

30. Mr. Banuri argued that the diagnosis of and proposed solutions for the economic difficulties facing developing countries have been misplaced. According to him, the problems of developing countries should be properly analysed in the context of a growing economic dualism, whereby the livelihood sector and corporate economy have diverged and become increasingly unconnected to each other. The solution to poverty eradication should be to revitalize this livelihood sector, where most of the poor are located, yet in practice, resources are being drained from here and flow instead to the corporate sector.

31. The policies of both the Bretton Woods institutions and the socialist model of economic development have failed to address this problem, according to Mr. Banuri. Moreover, the suggested solutions have wrongly focused on the need to increase the supply of resources for development, such as, for example, through increasing ODA. This ignores the fact that the existing resources around the world that are available for development are in fact quite large, especially with relation to the magnitude of poverty that exists. What is more essential is in fact the need to strengthen the access of the poor to these resources and to improve the utilization of these resources by both Governments and civil society institutions.

32. Thus, according to Mr. Banuri, the focus of the discussions on financing for development should be placed on the demand side, with a particular view to strengthening the abilities of the poor to demand and utilize existing resources. One proposed solution is sustained livelihood programmes. These programmes do not start from the basis that the poor are deprived of resources. Rather, employing microcredit and other tools, they aim to enhance the capacities of the poor to utilize existing resources. Examples of these programmes include measures to facilitate socially responsible investment and entrepreneurship, and to strengthen training and education programmes for the poor. Mr. Banuri recommended that a coalition of groups from around the world that have already engaged in these initiatives be formed and provided with the resources to broaden their work.

Maximizing the benefits and minimizing the costs of foreign direct investment: a gender perspective

33. Ms. Williams claimed that the assumption that trade liberalization and foreign direct investment will eliminate poverty and that foreign direct investment is not volatile and is inherently beneficial to recipient economies runs counter to actual experience. Moreover, gender has never been considered by policy makers as a core issue, although women are a key component of economic expansion given that they are the basis of the cheap labour that developing countries are endowed with and an important contributor to export expansion.

34. According to Ms. Williams, it is necessary to have a comprehensive assessment and reconfiguration of the trade and financial systems. Moreover, there is a need to highlight the interrelationships between gender, trade and foreign direct investment, and more broadly between economic growth and gender and between poverty and gender. When implementing trade or financial liberalization, gender and the general

dimension of sustainable development should be taken into account.

35. Ms. Williams enunciated some specific principles and recommendations. She stressed the need to restore the policy-making autonomy of Governments and to limit the rights of foreign investors. According to her, countries should have the right to protect their balance of payments, while Governments have the right to restrict imports and capital flows. At the international level, there is a need to cancel third world debt, to create a poverty eradication fund for developing countries, to promote the principle of differential treatment with regard to trade and investment rules, and finally to create supervisory mechanisms to oversee movements in capital.

Capital controls to reduce volatility and global financial turmoil

36. Ms. Ponti pointed out that the perceived virtues of globalization are far from being realized, partly due to the threat of volatile short-term capital flows, and made three specific recommendations. First, a global conference on financing for development should provide a seal of approval for countries to adopt capital controls during financial crises. In addition, although developing countries require long-term investment, standards should be set for foreign direct investment. Finally, policy makers around the world should pursue the idea of a small tax on currency transactions. This would serve many purposes, including reducing the volatility of external capital flows, restoring policy sovereignty in favour of the state and raising revenue for development purposes. However, this tax should not be employed as a mechanism to replace ODA. Ms. Ponti concluded her speech by stressing the need for a world conference on financing for development, which would involve ministers of foreign affairs, finance and trade.

Quality of African integration in the global system

37. Mr. Tandon's main argument was that the main source of financing for development in Africa must come from domestic savings. Aid, foreign direct investment and exports are less important sources. Moreover, it is false that there is a savings gap in Africa. This impression is created by the high rate of debt servicing in the region, which channels savings out of the continent. Therefore, instead of looking for outside funds to develop Africa, it is more important to find ways of stopping the seepage of funds from Africa.

38. According to Mr. Tandon, it is a myth to argue that open economies are more conducive to growth. It is also a myth to suggest that Africa must be more fully integrated with the global economy. The quality of integration is more important than the extent of it. Moreover, development cannot be reduced to finance. If finance comes to a country without bringing with it structural change, it can do more harm than good.

39. In sum, Africa should not open up its economies. It should realize that domestic savings are the primary source of growth, and in order to better utilize these savings it should implement structural change, not in the terms required by the Bretton Woods institutions but with relevance to its existing interrelationships with the global economy (for example, its terms of trade disadvantages). Finally, Africa must disown its debts.

Highlights of discussion

40. On the issue of debt, which was raised by a delegate and by the World Confederation of Labour, the possible consequences of debt repudiation by developing countries was addressed. Mr. Tandon admitted that the consequences of debt repudiation by the African countries could be sanctions. However, he felt that the damage could be limited if a large number of countries were to repudiate debt at the same time. Banuri, however, feared that debt repudiation could have a negative effect if it encouraged fiscal irresponsibility by Governments. For this reason, he felt that one has to approach this issue with caution.

Bretton Woods institutions

41. Another theme that received attention was the role of the Bretton Woods institutions, in particular views on how they should be reformed. Mr. Tandon argued that the existing Washington Consensus model preached by these institutions should be de-legitimized. In other words, the policy orthodoxy dictated by the World Bank and the International Monetary Fund (IMF) should not be blindly followed by developing countries, and moreover efforts should be made to confront the power of these institutions by, for example, creating regional financial mechanisms (as has, for example, been discussed in Asia). In response, a delegate argued that, even if the Bretton Woods

institutions were de-legitimized, whatever entity replaces them would still be driven by considerations of global politics and the vested interests of powerful member nations. Mr. Tandon, however, maintained that even if one accepts this point, the existing Bretton Woods institutions have become anachronistic, having been formed in line with the global conditions of the immediate post-war period, and are in need of significant reform.

42. Professor Banuri suggested that the role of these institutions be narrowed to the financing of large-scale infrastructure projects (in the case of the World Bank) and the maintenance of global financial stability (in the case of IMF). However, neither of these institutions should be involved in the area of poverty reduction and social objectives, nor should IMF provide policy advice and implement structural adjustment programmes.

Expert-driven model

43. A third issue that was discussed was whether the export-driven model adopted by Japan during the post-war era would be a prudent model for Africa to follow. The general view of the panellists was that Japan did not offer a model to Africa. First, global conditions at the time when Japan adopted its post-war development strategy were very different. In addition, conditions within Africa and its interrelationship with the outside world are very different from those that existed in Japan, not least due to the continent's experience with colonialism.

Strategies to reduce poverty

44. Strategies to reduce poverty were also discussed, in response to comments made by delegations. Mr. Tandon, Mr. Banuri and Ms. Williams argued that the poverty reduction strategies adopted by many countries at the behest of the Bretton Woods institutions were ineffective due to the arbitrary implementation of these strategies, their high costs and the overall policy and economic conditions brought about by World Bank/IMF programmes. The delegate from France argued that the elimination of poverty could be the focus for policy, but that this could best be implemented if there is unity among all the actors involved in this process. In response, Ms. Williams pointed out that different sets of actors have different views on how to eradicate poverty. Moreover, Mr. Tandon stressed that the existing global economic system is inimical to poverty reduction in the developing world.

Other issues

45. Two other issues discussed briefly were land reform (a question was posed by the representative of the National Union for Land Value Taxation) and the need for special and differential treatment of countries with respect to trade. Mr. Tandon argued that World Bank policies make it difficult to implement land reform. What is needed are outright measures that redistribute land to the tillers. With respect to trade, there was broad agreement on the need for special and differential treatment of countries.

46. Finally, there was a proposal from the floor by a civil society organization on a sustainable economic opportunities programme.

III. Increasing international financial cooperation for development through, inter alia, official development assistance; and debt

Moderator:

Asda Jayanama (Thailand), Co-Chair of the Preparatory Committee

Panellists:

Lidy Nacpil, Secretary-General, Freedom from Debt Coalition of the Philippines; and International Coordinator, Jubilee South

Vincent Edoku, Chairperson, Uganda Debt Network; and member of the Community Service Organization Poverty Eradication Action Plan Task Force

Rudolf Amenga-Etego, International Financial Cooperation for Development, representing the Executive Director, Integrated Social Development Centre

Jens Martens, United Nations Representative of the World Economy, Ecology and Development Association

Jenny Kimmis, Policy Department, OXFAM UK

Kunibert Raffer, Professor of Economics, University of Vienna

Increasing the consistency of financing and financial policies and processes with development principles and goals

47. Ms. Nacpil urged the United Nations to expand the scope for NGO participation in future activities, and made a number of points, as described below.

Debt servicing

48. The burden of heavy debt servicing and the urgency of releasing resources for development is not a problem of the heavily indebted poor countries (HIPCs) alone. Debt cancellation is needed and now by all countries of the South. Ms. Nacpil urged the United Nations to take a decisive role in challenging and changing the framework and instruments used to define indebtedness and debt sustainability, and in formulating alternative frameworks, concepts and instruments based on a more profound, critical, scientific, compassionate and just understanding of indebtedness and its extent and impact, and debt servicing. She asked the United Nations to direct appropriate agencies to work with civil society groups and grass-roots organizations for this purpose.

Debt cancellation

49. Debt cancellation should not be premised on compliance with economic policies and programmes that have been proven to have disastrous consequences for the economies of the South. Ms. Nacpil urged the United Nations to lead the call for the delinking of debt cancellation from economic conditionalities imposed by, prescribed by or identified with IMF and the World Bank; and to monitor and ensure compliance of Member States and IFIs with existing human rights norms and mechanisms (specifically in the context of how external debt and other economic issues and policies have led to gross violations of civil, cultural, political, social and economic rights, including the right to self-determination and development). She also urged the United Nations to form a global commission (with more than 50 per cent membership representing civil society) to critically review the work of IMF, the World Bank and other IFIs in order to determine whether they should continue to exist, and if so, to redefine the role they should play and if not to examine ways to de-commission them.

Debt legitimacy/illegitimacy

50. The debt problem involves the fundamental issue of the legitimacy and illegitimacy of debt. Ms. Nacpil urged the United Nations to make a decisive statement on the right of countries to non-payment of odious and illegitimate debts; to call for an immediate international investigation and inquiry of past and present illegitimate debts; and to establish mechanisms that will promote broad and critical interpretation and enforcement of an international law on odious and illegitimate debts.

Conclusion

51. Finally, she urged Southern Governments to form debtor coalitions and to repudiate debt.

The heavily indebted poor countries initiative and the Ugandan experience

52. Mr. Edoku used the Ugandan experience to illustrate that there are mismatches between domestic revenue and total expenditure, between exports and imports, and between economic and political mismanagement, and that there are problems of persistent shortages of foreign exchange resulting in problems servicing existing debt.

53. Although Uganda has been used as a model for sound macroeconomic management, it has not yet managed to translate this growth into improved living standards for the majority of the population. There have been problems with managing funds by the Government, and the terms of the borrowing are unfavourable.

Evolution of the debt situation

54. Heavy borrowing occurred during 1981/85, and after 1987. Problems included poor management, unfavourable borrowing terms and no debt-servicing policy.

Lack of progress in managing debt

55. From 1980/81 to now, efforts continued to help manage the debt, including debt verification exercises, debt rescheduling agreements, installation of debt recording and loan administration systems, and elaboration of debt management strategies. The debt stock was still at US$ 3.6 billion in 1998, and debt servicing reached US$ 163 million.

Initiatives to reduce high levels of indebtedness and poverty

56. A poverty eradication action plan was launched in 1997, directing the use of public resources for poverty eradication. The first phase of the HIPC initiative provided hope; in 1998, debt in terms of net present value was reduced from US$ 1,748 million to US$ 1,401 million, and debt servicing fell by an estimated US$ 41 million. The Government established a poverty action fund to channel savings from the first phase of the HIPC initiative to priority poverty reduction programmes in the plan. Now, the 1997 plan is being revised, decentralization is under way and the Uganda participatory poverty assessment project was launched in 1998. Uganda became the first country to receive debt relief under the second phase of the HIPC II initiative, in 1999. Together, the first and second phase of the HIPC initiative will have reduced overall debt stock from US$ 1,748 to $745 million in net present value terms, and reduced debt servicing from US$ 149 million to US$ 62.5 million in 2000/01. The poverty action fund is expected to grow from US$ 96.7 million in 1998/99 (22 per cent of budget) to US$ 447.68 million in 2002/03 (32.2 per cent).

More debt?

57. It is disheartening, however, that a new credit from the World Bank for poverty reduction (poverty reduction support credit) is already under discussion, although it is unclear whether this comes as a direct result of the HIPC cancellations.

Key points

58. The Ugandan Government and civil society must:

(a) Avoid policies that will take them back into another debt crisis;

(b) Improve governance and accountability in the use of public resources;

(c) Ensure donor coordination and partnership. Donor assistance strategies should be designed to support existing strategies and channel any funds through the budget;

(d) Emphasize that conditionalities and agreements should be enforced once agreed upon, to ensure funds are used for the identified programmes as agreed;

(e) Open up the political space for alternative views;

(f) Update legislation to regulate external borrowing and loan terms (only concessional);

(g) Create a debt coordinating agency and scrutinize all borrowing to ensure that it is needed and that the Government can service it;

(h) Seek endorsement of HIPC-type instruments by all creditors and donors. In the final analysis, the promotion and diversification of exports to minimize instability of export earnings, particularly in agriculture, is the only way out of the recurrence of debt.

Critical question

59. With the first and second phases of the HIPC initiative and with the poverty reduction strategy credits, are Uganda's debt problems over?

International cooperation, official development assistance and debt

60. Mr. Amenga-Etego spoke of the problems associated with having one dominant ideology with its "one hat fits all" approach, which is socially unjust, ecologically destructive and violates the core principles under which the United Nations was born. The financing for development process offers an opportunity to construct alternatives: this requires bold ideas with far-reaching consequences for the organization of social life, economic enterprise and the role of the state. An examination of financial cooperation should answer the question: "How should the financial system be structured and managed to ensure that financial resources are available in non-sexploitative ways to finance human development worldwide in a predictable and stable manner?".

Development cooperation today

61. Development cooperation has reduced the more far-reaching goals and ideals of international cooperation — maintenance of peace, pursuit of prosperity and dignity of all life without regard to sex, race, religion or culture, equality of humanity and pursuit of orderly exchange of knowledge and cultures — into a narrow discourse on aid effectiveness. Core values and beliefs underpinning human relations disappear; now institutions that convey and mediate aid

have become more powerful than the purpose and values underlying their creation. The arena is now characterized by asymmetrical power relations between "giver" and "receiver"; this has affected NGOs, which can help perpetuate this asymmetry. The basis of NGO engagement has eroded: we mobilize sympathy rather than organize for political change. Therefore, we must return to our roots. The depoliticization of poverty has ensured that the institutions, political arrangements and ideas inimical to the rights of the poor are getting stronger and more heartless.

Reality of aid and relationships within the aid industry

62. Much has been written about declining aid flows; paradoxically, as fewer resources are transferred from North to South, the influence of Northern-dominated institutions is more pervasive. The asymmetry takes several forms, controlling flows and sanctioning those Governments that diverge from the dominant paradigm. The subtle control of ideas, information and analyses generates the perception that for knowledge to be legitimate, it has to meet Western standards. Thus, the World Bank attempt to corral ideas into one coordinated framework through the global knowledge gateways and networks is insidious and should be opposed. Diversity in terms of ideas is essential. The comprehensive development framework claims to promote partnership but ignores asymmetrical power relations.

International financial institutions

63. Key decisions should not be made in the absence of the people (*you cannot shave a person's hair in his/her absence*). The World Trade Organization (WTO) is the greatest promoter of undemocratic decision-making and is the face of neo-colonialism (*at the tribunal of the foxes, the chickens are always guilty*). There is a gaping chasm between the participatory rhetoric of the IMF/World Bank and their operations on the ground, as evidenced by their poverty reduction strategy papers.

Poverty Reduction Strategy Papers

64. Poverty reduction strategy papers (PRSPs) represent a power shift from Governments of low-income countries to IMF and the World Bank, including the endorsement of national strategies that fall under the sovereignty of the state. They "manufacture consent" for the Washington Consensus, which has been promulgated through structural adjustment programmes for 20 years, with negative consequences, especially for low-income countries. They expand the micro-management of poor countries by IFIs and although they appear benign, they contain forces of destruction, offering too little assistance too late to the poor.

Policy recommendations

65. It is inappropriate for IMF and the World Bank to endorse national strategies; PRSPs should not be considered national strategies, nor should they be linked to the debt reduction process. Structural adjustment programmes should be transformed and scaled down or discontinued. Citizens' groups have a legitimate role in discussing macroeconomic and structural policies. Transparency on the part of IMF, the World Bank and borrowing Governments is essential.

Debt cancellation/reduction

66. Inherited bad debt, onerous and illegitimate debt should be cancelled in the spirit of social justice. No serious initiative exists to address the debt burdens of middle-income countries. ODA should not be diverted to service debt. Debt relief arrangements, such as the HIPC initiative, are inadequate and in some cases usurious. An independent international debt tribunal is needed to determine the legitimacy of debts and their eligibility for write-offs. Debt-distressed countries should enjoy the benefits of insolvency. The United Nations Conference on Trade and Development (UNCTAD) supports a six-point debt work-out strategy, including (a) a temporary standstill on payments, without capitalizing interest as it comes due; (b) continued financing during this period, and (c) debt restructuring that does not privilege the creditor.

Changing rules for international finance

67. The system must generate adequate and appropriate resources for investment where it is most needed, and be reasonably able to prevent crises and, when crisis breaks out, to manage the impact while minimizing the cost to the poorest and most vulnerable.

68. The financing for development process should give serious consideration to proposals that involve:

(a) National implementation of a currency transaction tax;

(b) Capital controls at the national level, where appropriate;

(c) Increased transparency and regulation of investors, especially hedge funds;

(d) Management of exchange rates;

(e) Coordination of macroeconomic policy to support exchange rate targets and promote sustainable development and full employment;

(f) Strengthening existing regional and subregional institutions and the creation of new ones, such as regional monetary funds;

(g) The abandonment of compensatory measures, combined with onerous debt servicing, have left poor countries unable to survive without concessional financing. But this financing can exacerbate the problems it aims to address unless the following strategies are followed at the national level: policies supporting investment in local production; fair and efficient taxation; creative local credit generation; incentives for reinvestment of profit and discouraging luxury imports; effective management of foreign exchange; anti-corruption measures; civic consciousness to force transparency and accountability and provide oversight over budget policy alternatives that enhance domestic resource mobilization without neo-liberal orthodoxy; and industrial strategies that support and provide incentives for building key strategic industries. This also requires restraint on the part of IMF and the World Bank from promoting capital account liberalization; restraint on the part of IMF from including exchange rate regimes as part of conditionality; and the pursuit of proposals to hold reserves in domestic financial markets rather than abroad.

Solidarity as an alternative framework for collaborative action

69. Solidarity produces progressive, transparent and egalitarian outcomes; there is less ambiguity about power relationships; and it represents shared values and interests but makes no pretence of sharing interest at all levels. It is clear that what is needed is a human-rights-based framework as a basis for international action.

The future of official development assistance: a global partnership

70. Mr. Martens spoke on overcoming the crisis of official development assistance, and the case for a global development partnership agreement. There is a broad consensus in the development community that ODA is one of the important financial instruments for fighting poverty and promoting sustainable development in the South, and cannot substitute for debt relief, improved trade conditions etc. ODA is needed because blind faith on private flows or markets leads to undesirable results. The challenge for the financing for development process is to offer a solution to the impasse in North/South negotiations on finance.

Crises

71. ODA is declining: contributions by all Organisation for Economic Cooperation and Development (OECD) countries fell from US$ 59.6 billion in 1994 to $49.7 billion in 1998 (from 0.3 to 0.24 per cent of gross national product (GNP)). OECD/Development Assistance (DAC) concludes that, from 1992 to 1998, there was a net loss of US$ 88.7 billion, a figure which is well over US$ 100 billion by now. Unfortunately, donors are not addressing quantity issues but are instead:

(a) Emphasizing quality of assistance, whereas they need to increase quantity and quality;

(b) Concentrating on selected recipients, showering "models" with resources while excluding others;

(c) Focusing on public-private partnerships, which are sometimes but not always sensible.

Policy recommendations

72. The financing for development process could:

(a) Start an official negotiation process to the formulation of a new development agreement along the lines of the anti-poverty convention discussed in Geneva at the five-year review of the World Summit for Social Development. Reaching the international development targets could be linked to such a convention;

(b) Analyse the feasibility of inter-country income transfers or state financing offsets at a global level (e.g., a progressive income tax of rich countries)

to increase the reliability of official resource pledging and ease long-term development planning in the South;

(c) Targets for ODA assistance should depend on the real financing needs of recipient countries, resulting in needs-based targets for ODA rather than the target 0.7 per cent of GNP;

(d) To avoid further indebtedness of recipient countries, development assistance should be in non-repayable grant form; the United Nations should undertake further studies on the economic and social impact of loan-based ODA;

(e) Revitalize the role of the United Nations as the main body for decision-making and policy coordination. This will require institutional reforms and a new division of labour between the United Nations, the World Bank and IMF in global development finance, with the United Nations as the undisputed lead agency.

Conclusion

73. The financing for development process offers the historic opportunity to give a signal of global solidarity towards a new North-South partnership.

Tax havens

74. Ms. Kimmis spoke on tax competitions and tax havens, and on debt and liquidity crises in non-HIPC countries, both of which are inadequately addressed under the current system of global economic governance.

Tax competition and tax havens

75. One third of global GDP is now in financial havens, much of which is undisclosed and untaxed, and the rest under-taxed. Oxfam estimates the annual revenue losses for developing countries are, conservatively, at least US$ 50 billion.

76. Offshore centres undermine the capacity of poor countries to finance sustainable development in three ways:

(a) Tax competition and tax escape: tax havens and tax competition in general provide opportunities for wealthy individuals and businesses to escape their tax obligations, and force developing countries to progressively lower corporate taxes on foreign investors;

(b) Contribution to rising incidence of financial crises: foreign exchange traders and globally active private financial institutions use havens and offshore centres as booking centres for short-term and speculative investments in developing and transition economies;

(c) Providing a safe haven for proceeds of illegal gains from political corruption, illicit arms dealing, illegal diamond trafficking and the global drug trade: ongoing initiatives focus primarily on the concerns of Northern Governments and lack a development perspective.

77. Four policy options could help the international community deal with these problems:

(a) Signing a multilateral agreement to share information on tax matters;

(b) Supporting the proposal for an international convention to facilitate the recovery and repatriation of funds illegally appropriated from national treasuries of poor countries;

(c) Agreeing to allow States to tax multinationals on a global unitary basis, with appropriate mechanisms to allocate tax revenues internationally and help avoid transfer pricing abuses;

(d) Setting up a global tax authority to gather information, serve as a forum for discussing international tax policy issues, use peer pressure to bring tax-free riders into line, and develop best practices codes of conduct on tax issues.

Debt and liquidity crises

78. With the opportunity that many developing countries have to tap into external sources of credit come rising levels of external debt owed to private creditors. The latter is becoming increasingly short term and spread among a diverse group of creditors. There are no clear rules on how the international community should respond.

79. Oxfam believes that multilateral rules on debt restructuring are needed that are based on:

(a) Repayment capacities of the debtor country, including human development needs;

(b) A transparent trigger mechanism based on a range of debt and development indicators.

Any low- or middle-income country that meets these criteria would have the right to seek assistance through

an international debt restructuring initiative. These principles could be supported by a set of procedures similar to bankruptcy provisions at a national level. Thus debtors would avoid often brutal adjustments and long delays in debt restructuring; debtor moral hazard would be minimized as this gives a right, not an obligation, to seek assistance; comparable treatment of creditors would ensure that official and private creditors share the burden fairly; and it would reduce the need for debt write-downs at a later stage.

Fair and open process of arbitration to solve the debt problem

80. Mr. Raffer explained how history shows that protracted manoeuvring cannot force the payment of unpayable debts; all it does is increase the debt overhang, adding debts that can never be repaid but burdening the debtor. Aid money often gets diverted to "maintain" debt service payments that countries cannot make by themselves.

81. British and French Governments defaulted in the 1930s, considering the needs of their peoples more important than legal obligations to creditors. United States states have a long history of defaulting; Germany, Indonesia and Poland have all been granted partial debt cancellations in the past; the Egyptian debt crisis of 1876 was managed by private creditors, who used the domestic bankruptcy law as a basis — this was economically successful for both debtor and creditors alike after a surprisingly short time.

Who decides?

82. Who decides how much can be repaid, how much protection the poor should get and what investments are needed to keep the country going? So far, creditors alone decide reductions with dire consequences for debtors. But the most fundamental principle of rule of law is that one cannot be judge in one's own cause.

Phantom debts

83. Creditors unwilling to grant sufficient relief when necessary increase their irrecuperable credits. Claims keep growing on paper, going further beyond the debtor's economic ability to pay, resulting in "phantom debts", existing only on paper. Deleting these debts is simply acknowledging the economic fact that these are funds the creditors cannot get.

Basic insolvency procedures

84. Basic insolvency procedures solve the conflict between (a) the right of bona fide creditors to interest and repayments and (b) the right that everyone has not to fulfil contracts if that leads to inhumane distress, endangers one's life or health or violates human dignity. This does not apply to odious debts, where no insolvency is needed, as they are null and void.

Can these procedures be used in cases of sovereign debt?

85. Although the rule for the insolvency of firms cannot be applied (as in United States chapter 11 bankruptcy laws), United States chapter 9 bankruptcy procedures show principles of justice and fairness can be implemented using arbitration. This principle, used in the United States for decades as the solution to the problems of municipalities, can apply to sovereign borrowers because it protects creditors' rights as well as both debtor's powers and the living standards of the population. It also ensures that individuals affected by the decision have a right to be heard.

Arbitration

86. Internationally, a neutral arbitration panel should be constituted, with each side nominating an equal number of arbitrators, who in turn elect one more member; these panels would be dissolved after their job is done. Arbitration is increasingly applied to international problems, including the North American Free Trade Agreement (NAFTA) or WTO; the London Accord with Germany (1953 etc.). The population can exercise its right to be heard by being represented by NGOs, trade unions, employers' association, grass-roots organizations, or international organizations, such as the United Nations Children's Fund (UNICEF). The United Nations can serve as the organization where such sovereign debtors can file their requests for arbitration, fairly balancing the interests of creditors and debtors, organizing the nomination of arbitrators and perhaps providing limited secretarial services for arbitrators.

Minimum protection

87. Protection of a minimum standard of life should be a part of every international plan. Basic human services must not be destroyed; subsidies and transfers necessary to guarantee humane minimum standards for

the poor must be maintained; and funds needed for sustainable economic recovery must be set aside. A transparently managed fund (as proposed by Jubilee 2000), financed by the debtor in domestic currency, would ensure that exempted money is used for the poor and for economic recovery, monitored by an international board with debtor and creditor membership.

88. Such arbitration, modelled after United States chapter 9 bankruptcy laws, would fulfil the demands of donor Governments — participation, transparency and respect for the rule of law — and would provide a disincentive to careless lending. It would also maintain both human rights and the rule of law for the debtor nations. No difficult or costly legal or administrative framework is necessary.

89. People in debtor countries need justice and economic sense, not generosity — and the same protection of their basic needs and human dignity that any other debtor already enjoys. The criterion is simple: "Everyone who looks like a human being should be treated like one".

Highlights of discussion

Official development assistance and debt

90. One delegate asked how can we analyse the underlying causes of indebtedness, and Ms. Nacpil replied that knowing and understanding the historical causes of debt is key to finding a solution and addressing strategically the vicious cycle of debt. The same delegate asked whether in countries that are ruled according to Roman law insolvent people are deemed uncreditworthy. Mr. Raffer answered that nothing about being insolvent precludes access to credit — if creditors see an opportunity, they will come. Also, arbitration is part of Roman law. On the role of debt, one participant noted that solutions existed in 1982, when Mexico, Brazil and Argentina were in crisis, but they were ignored.

91. One delegate asked how we could ensure that debts would not recur. What can we expect from Governments? Mr. Raffer answered that international arbitration will force creditors to look closely at how money is being spent before lending. Mr. Amenga-Etego stressed that Governments should be transparent and accountable to their own people, and should put into place laws to punish corruption and recover stolen funds. Political rights should also be denied to convicted corrupt officials. Ms. Nacpil said that creditors know they are lending to corrupt Governments, so the people do not need to pay. Continued borrowing to remain afloat will not end unless the debts are repudiated. Southern Governments should stop implementing IMF economic programmes.

92. The International Association Against Drug Trafficking called the meeting's attention to item 17 of the IMF communiqué from its Prague annual meeting, at which IMF and the World Bank promised to come up with a position on international crime and trafficking by its spring 2001 meeting, and urged all NGOs to focus on this. He also stressed that we are running the risk of institutionalizing current crimes and trafficking and corruption by being so kind as to forgive debt, as if people were being robbed twice. The panel agreed that on the institutionalization of crimes, local guilty parties would be held accountable by the people but the double crime is when people are robbed once by corrupt officials and then again when they are forced to repay the debts.

93. Mr. Edoku noted that in debtor countries, there has to be a needs assessment of what the money is being used for before funds are borrowed, and the borrowing terms have to be good. Mr. Raffer added that debt arbitration is not about kindness and should not be seen as such, it is simply common sense. The moderator concurred with Oxfam's analysis and asked that they and others help find out how much money is held offshore.

94. Mr. Martens noted that donors have several ways to react to debt crises. In many cases, bilateral creditors have cancelled loans. There are also serious ongoing discussions on how to solve debt crises at that level. The international courts in the Hague could conduct arbitrations.

95. From the floor, the Catholic Relief Services representative observed that the solutions given here for corruption all happen after the fact, and asked if there are ways to punish the corrupters as accomplices to these crimes.

96. Mr. Amenga-Etego stressed that Governments' accountability to the people will stop corruption worldwide. We need to focus on non-developing nation creditors, transnational corporations etc. We need to set up international tribunals for corrupt leaders and corporations. Intelligence agencies, too, should come

forth and provide what information they have to protect humanity.

97. One delegate made a comment on United States chapter 11 bankruptcy laws and arbitration, which have been on the table for a long time, but all creditor countries have been silent on these issues. Why is this? Mr. Raffer said that there is no logical answer to that. Chapter 9 bankruptcy laws are a better instrument in any case since they give populations the right to be heard.

98. The moderator called on the IMF representative to discuss issues related to IMF conditionalities, economic policies etc., and the IMF representative said that the same Governments that are creditors and debtors are also the governing body of IMF; so rather than blame innocent officials, those who do not agree with the policies of these Governments, should take it up with them.

99. The Global Policy Forum observed that the problem of lending into corrupt situations can also include lending by IFIs to corrupt situations, such as an IMF loan to an unnamed country that was followed immediately with a large deposit offshore. How can IFIs and individuals within those IFIs be held accountable for those types of loans? Mr. Raffer replied that national sovereignty is compatible with arbitration: in the case of NAFTA, Canadian law or American legislation can be overruled. So bring the market to IMF — they should shoulder the financial consequences of bad lending. Ms. Nacpil added that people of the South should refuse to pay as a first step — shut down IMF if it is not playing the role that you want it to play. The IMF representative noted that recently at meetings held in Prague these same Governments came together but they did not raise these issues.

100. The representative of Earth Rights and others agreed that there is another approach to wealth creation, as 80 per cent of the world's land and natural resources is in the hands of 5 per cent of the world's population. Taxation could help to generate new funds.

Trade

101. Debt and trade problems are intimately related. One participant added that the causes of debt must be analysed to avoid recurrence:

(a) Loan pushing by creditors occurs and is unethical;

(b) Structural problems exist: they are built into the trade system, which perpetuates trade deficits between well-off and poor countries, the only solution for which is debt. This imbalance needs to be rectified;

(c) Declining terms of trade cause debt;

(d) Goods valuation means that Northern goods (such as Coca Cola) can have sharply rising prices but Southern products (such as oil) come under attack.

102. The World Confederation of Labor raised the following questions:

(a) Do you consider the recent cooperative agreement between Cuba and Venezuela, trading services of health professionals for oil, as a good model of South-South collaboration?

(b) If IMF and World Bank are seen as obstacles to development finance, will the High-level Event make a statement to that effect?

(c) IMF Managing Director Köhler in Prague, together with World Bank President Wolfensohn, supported increased trade access for developing countries. This could possibly lead to US$ 100 billion in income for developing countries. How do the European panellists feel about the likelihood of this happening?

(d) Guyana was on the list of 10 original HIPC countries but was dropped because of its decision to increase salaries to civil servants in order to avoid civil (racial) unrest and give a living wage to its African workers. Should the HIPC initiative look at social and ethnic matters in addition to financial ones when deciding to provide debt relief?

103. Mr. Martens answered by saying that the European Union (EU) opened its markets to the South, but this should not have been reciprocal, i.e., Southern Governments should be able to protect their markets. There is still a need for special and differential treatment. Oxfam believes in opening up markets and is about to launch a campaign to that effect.

IV. Addressing systemic issues: enhancing the coherence and consistency of the international monetary, financial and trading systems in support of development

Moderator:

Jørgen Bøjer, Co-Chair of the Preparatory Committee

Panellists:

Kandeh Yilla, Secretary-General, Sierra Leone Labour Congress; member, International Confederation of Free Trade Unions

T. Rajamoorthy, Senior Adviser, Third World Network; Editor, Third World Network Resurgence

Doug Hellinger, Executive Director, Development Group for Alternative Policies; Global Coordinator, Structural Adjustment Participatory Review International Network

Humberto Campodonico, Centro de Estudios y Promoción del Desarrollo

Alfred Pfaller, Policy Analysis Unit, Friedrich Ebert Foundation

Jocelyn Dow, President, Women Environment and Development Organization Board of Directors

Defining the institutional policy environment to harness resources for development

104. Mr. Yilla, identified two main goals for the financing for development process: the creation of the appropriate institutional and policy environment for social development; and the effective harnessing of resources for development.

105. Enhancing the consistency of the international monetary, financial and trading systems means ensuring that policies formulated within those systems are consistent with the outcome of sustainable development, including poverty reduction, employment growth and social protection. It also means that these social outcomes should be built into the design of policies. As a consequence, austere policies prescribed by IMF need to be revamped. Consistency also requires effective mechanisms to prevent systemic crises, which hurt workers and the poor more than capital markets and investors.

106. Effective intergovernmental cooperation is essential, and should be enhanced by a strengthened coordinating role of the Economic and Social Council, bringing together the United Nations specialized agencies with the Bretton Woods institutions and WTO.

Policy recommendations

107. To harness resources for development in the framework defined above, the financing for development process should focus on the following areas: an international tax on foreign currency transactions; regulation of hedge funds and off-shore financial arrangements; burden-sharing by commercial banks during debt crises, including standstill arrangements; deeper and broader debt relief under a vastly improved HIPC initiative; and a timetable for donors to reach the United Nations ODA target of 0.7 per cent of GDP.

108. With respect to trade, the High-Level Event should consider greater market access for developing country products; inclusion of social policy consideration in the world trading system; and measures to ensure that globalization does not lead to negative outcomes in the areas of development and equity, including fundamental workers' rights.

Financial liberalization

109. Mr. Rajamoorthy focused on the issue of financial liberalization. Recalling the damage that such policy — strongly advocated by IMF — had caused to the countries hit by the Asian crisis, he put forward two sets of proposals. The first involved the need to avoid further financial liberalization, including an end to the pursuit by IMF of amendment of its articles of agreement 1 and 8, to enable it to push developing countries to open up their capital account and markets; an end to any attempt by OECD to revive the proposed multilateral agreement on investment, which would give unfettered freedom of mobility to all types of capital flows, and to similar proposals under the aegis of WTO; a review of the financial services agreement in WTO to take into account the lessons learned from the negative effects of financial liberalization resulting from the latest round of financial crises.

110. The second set of proposals related to needed international policies, including effective crisis

management measures, such as debt standstill arrangements, debt workouts and an international version of United States chapter 11 bankruptcy laws, aimed at fair burden-sharing; a framework for the introduction of capital controls; regulation of institutions in the countries that are the source of mobile financial funds, aimed at preventing them from creating excessive volatility; international regulation of hedge funds and other highly leveraged institutions, off-shore centres, currency markets and derivatives; consideration of a more stable currency system (including a return to fixed exchange rates or bands); a reform of the decision-making system in such international institutions as IMF to give developing countries a fair say in their policies; and a change in the set of IMF-World Bank conditionality.

111. Unilateral actions in the area of financial and trade controls would be warranted in developing countries in the absence of implementation of the above measures.

Changing the nature of decision-making

112. Mr. Hellinger rejected the possibility of enhancing an international system that, in his view, has not been supportive of development in the past. On the contrary, the imposition of structural adjustment programmes has undermined democratic processes, increased poverty and inequality, and generated social, economic and financial instability. Mr. Hellinger challenged the leaders of the United Nations and its specialized agencies to converge around a different set of values and principles, including respect for diversity, equity, self-reliance, self-determination, environmental sustainability, democratic decision-making, and transparency and accountability, and to change the nature of global decision-making. A new partnership between their institutions and civil society movements was required, to launch a parallel process to the flawed PRSPs to look at the poverty effects of adjustment programmes. Progressive Northern Governments should help the United Nations finance these national exercises, thereby strengthening the role of United Nations agencies in promoting equitable economic and social development.

New development strategy to counter the Washington consensus

113. Mr. Campodonico denounced the absence of an international monetary system since 1971 and its negative consequences, especially on developing countries, as well as IMF's inability to fulfil its surveillance mandate. In view of the surge in international capital flows, controls and regulation of offshore centres were urgently required. Mr. Campodonico added his voice to the criticisms of structural adjustment programmes based on the Washington Consensus, and suggested four issues for discussion at the High-level Event: global implications of exchange rate movements of major currencies for other countries; unequal distribution of voting power in the global financial system; governance of IMF, where few countries have undue influence on the decision-making process; and insufficient transparency and accountability in capital markets and institutions of developed countries. He also called for a new development strategy alternative to the Washington Consensus to challenge the neo-liberal paradigm.

Policy priorities on the way towards a new international financial architecture

114. Mr. Pfaller stressed the need to strengthen the international financial architecture to reduce the likelihood and severity of new financial crises. New measures are being developed within the framework of the Financial Stability Forum, aimed at enhancing transparency in global financial markets; improving prudential regulation of international financial transactions; strengthening financial institutions in emerging market economies reducing "moral hazard" for reckless investors. However, they are insufficient.

115. More far-reaching proposals advanced by several academics, focusing on a more encompassing regulation of capital flows, reduction of flows and stabilization of currencies, are unlikely to be implemented. Hence, in the absence of a new financial architecture, available policy options should be considered. Sound macroeconomic policies and strengthened financial institutions are necessary but insufficient to immunize countries from financial vulnerability. One reason is contagion, owed to investors' tendency to herd behaviour in volatile markets. Another was boom-bust cycles in developing countries associated with inflation and interest rate differentials and currency misalignments. To reduce the likelihood of the latter, either capital controls or fixed exchange rates are necessary. Controls seem to be the preferable option, although they entail foregoing the benefits of open capital markets, such as lower cost and

better allocation of capital. Yet these trade-offs seem acceptable, as confirmed by the record of some of the best performing developing countries, which kept capital control until recently.

Mobilizing financial resources for women and girls

116. Ms. Dow noted that financing for development ultimately means mobilizing financial resources. It was less a matter of quantity of resources than of their fair distribution. The neo-liberal model that is at the core of the current global monetary, financial and trading systems, as well as the institutions that shape them and set the development agenda, do not work for women and girls. Extreme female under-representation in national and global decision-making is alarming. Ms. Dow put forward four sets of recommendations: (a) transforming institutions and Governments; (b) transforming their policies; (c) targeting more money for women and girls; (d) taking control of these funds.

117. An approach similar to the Women Environment and Development Organization (WEDO) campaign for gender equity in national Governments should be applied to multilateral institutions. Also needed were procedures to allow for more transparent NGO participation in the crafting and evaluation of policies of multilateral institutions, including the United Nations. With respect to transforming policies, WEDO has called for debt cancellation for Africa across the board, elimination of adjustment conditionalities from the HIPC initiative and strengthening of effort by United Nations agencies to reform definition and measures of development, to incorporate gender and environmental concerns. WEDO also supports the call for reaching the ODA target of 0.7 per cent of GDP, and within increased development assistance resources, proposed to set a target of 50 per cent of funds allocated to projects directly benefiting women and girls. Similarly, high targets in favour of the same cause should be set by World Bank and United Nations specialized agencies. Moreover, WEDO is in favour of such instruments as the Tobin tax on international currency transactions and pollution taxes. Finally, targeting resources to meet the needs of women and girls is a necessary step that needs to be coupled with increased accountability and transparency, to ensure that funds were used the way they were intended.

Highlights of discussion

Role of the United Nations

118. Several interventions stressed the importance of bringing back to the United Nations the economic and financial debate in order to define a reform agenda and to promote a more just globalization process. The United Nations is also seen as the appropriate forum for NGOs to discuss economic and financial issues.

Reform of the Bretton Woods institutions and their engagement in the financing for development process

119. A combination of "reason plus pressure" was suggested to effectively influence the Bretton Woods institutions policies, as their closure would be counterproductive, though advocated by some. Excessive demands for radical changes risk leading to isolation of NGOs. Despite their poor track record, it is essential to engage the Bretton Woods institutions in the financing for development debate. An open and responsible discussion of practical issues would make a successful event.

Transnational corporations

120. The need for a discussion within financing for development of the role of transnational corporations in development was stressed, as ICFTU pointed out that their impact in many developing countries had been even worse than that of the Bretton Woods institutions.

Digital divide

121. The implications of the revolution associated with the explosion of information technology, and the related issue of the digital divide should be included in the financing for development debate. There were indications that the development of the New Economy had not reduced inequality.

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Financing for development: hearings with the business community, 11 and 12 December 2000

Summary of panel presentations and discussion

Summary

In its resolution 54/279, the General Assembly decided that the Preparatory Committee for the High-level International Intergovernmental Event on Financing for Development would hold two sets of hearings with civil society organizations and the business community to consider their views on areas of the financing for development agenda. On 11 and 12 December 2000, business hearings were held in New York; the present document summarizes the presentations made by 17 senior business representatives, and provides a synopsis of the dialogue among delegations, speakers, international agencies, civil society and other business representatives.

The main areas of discussion were:

(a) Mobilizing domestic financial resources for development (sect. I);

(b) Foreign direct investment, project finance and venture capital (sect. II);

(c) Other private capital flows (sect. III);

(d) Trade, systemic and other issues (sect. IV).

The statements made at the hearings are available on the Internet at:

http://www.un.org/esa/ffd/NGO/1200hear/panel_list2.htm

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I. Mobilizing domestic financial resources for development

Moderator:

Jørgen Bøjer (Denmark), Co-Chair of the Preparatory Committee

Panellists:

John de Wit, Managing Director, Small Enterprise Foundation, Northern Province, South Africa

Chulakorn Singhakowin, Chairman of Thai Bankers Association and President/CEO of Bank of Asia Public Company Limited, Bangkok

Victor Valdepenas, President, Union Bank of the Philippines, Manila

Hernan Somerville, Managing Director and Shareholder of Fintec, Santiago

Supportive regulatory policies for microcredit

1. Mr. de Wit presented recommendations on government policies that are supportive of the development of microcredit. His discussion was based partly on the experience of South Africa, and more specifically on the experience of the Small Enterprise Foundation. The Foundation is a South African microcredit organization targeting the rural poor, focusing on financing microenterprises, with a mission of eradicating poverty. Only about 10 per cent of clients expand beyond the microenterprise level and leave the informal sector.

2. His first recommendation highlighted the importance of relaxing general restrictions on lending activities and raising interest rate ceilings on microcredit loans. The latter should be permitted to be 75 to 100 per cent above the prime lending rate. Protection of borrowers from exploitative charges can be accomplished by instituting consumer protection measures. At issue here is the sustainability of microcredit organizations, which depends on the ability to charge interest rates that are adequate to cover high operating costs and provide a small profit.

3. The second recommendation stressed the development of savings and insurance services for the poor, which are needed to reduce their vulnerability to shocks and large life cycle expenditures, such as weddings and funerals. In many countries, savings services for the poor are provided by postal savings system. This function should be preserved while other institutional arrangements are being developed.

4. Mr. de Wit also emphasized that the Government needs to implement policies to create a supportive environment for the development of microcredit. These should be based on a long-term strategy, with a time horizon of 10 years, which recognizes the need to develop the requisite skill. The strategy should aim to strengthen existing microcredit organizations and create a number of new institutions so as to establish a critical mass of viable institutions that can produce large-scale delivery of services. The process should be free of political interference or politically driven delivery objectives. The Government should also provide funding for the development and expansion of microcredit institutions and accord priority to such expenditure.

5. Mr. de Wit underscored the fundamental difference between the business of commercial banks and that of extending microcredit. Therefore, he cautioned against pressuring commercial banks to enter the microcredit field. Rather, he favoured focusing on facilitating alliances between banks and microcredit agencies, with an emphasis on developing transparency and strong governance of the latter to make them good clients for commercial banks.

Dialogue

6. In response to questions from participants, Mr. de Wit attributed the disincentive for commercial banks to be involved directly in microcredit to the lack of collateral and formal accounting records in microenterprises, which increases their riskiness as clients.

7. On the desirability of government funding of microcredit organizations, some participants differed from Mr. de Wit, pointing out the risks of corruption and government and/or Central Bank restrictions on operations. Participants also discussed the possible role of donor Governments and international organizations in the development of microcredit. Mr. de Wit alluded to a loan that the Small Enterprise Foundation secured from a Dutch bank with a foreign exchange risk guarantee provided by a Dutch government-funded organization. In addition, he cited successful cases of direct funding by bilateral donor agencies, where they identified and funded local microcredit organizations perceived as potential "leaders" or "winners".

Financial restructuring in Thailand

8. Mr. Singhakowin's presentation focused on the progress of financial sector restructuring in Thailand and further measures that are necessary to expedite the process. The financial crisis, which erupted in 1997, was the result of a long period of high investment and rapid economic growth, supported by strong expansion of lending by domestic banks and offshore borrowing. Some of the easy financing fuelled speculation in real and financial assets, resulting in a sevenfold increase in the stock market index and a quadrupling of real estate prices in the decade preceding the crisis.

9. As a consequence of massive deposit withdrawals and loan defaults in the wake of the financial crisis, the share of non-performing loans in the banking sector increased to 48 per cent of all loans by mid-1998. A large number of non-bank financial institutions and a number of commercial banks failed. In response, the Government committed to a market-led strategy to restructure the sector. This involved efforts to assist financial institutions in restructuring, including the strengthening of regulations; reform of institutions and the legal framework for settling insolvency and bankruptcy; creating an agency to assist in debt restructuring; and tax adjustments to enhance the process. Bank regulations were tightened to force recapitalization of the remaining institutions. Restrictions on foreign ownership of Thai banks were eliminated to allow full foreign ownership in order to facilitate the inflow of capital to the sector.

10. These measures have resulted in consolidation of the sector and greatly reduced the likelihood of more bank failures. However, lending activity in the sector has not been revived because of the need to increase provisions for a still very high level of non-performing loans (30 per cent). The slow pace of clearance of non-performing loans can be attributed to the still inadequate institutions and legal framework for resolving problem loans or preventing new defaults, which has in turn deterred prospective domestic and foreign investors from placing new capital in the sector. Further strengthening of the institutions and legal framework to resolve bad loans in a manner that creates a better balancing of risk-sharing will be needed to promote the recapitalization of banks.

11. In response to the slow progress in recapitalization of banks, there has been increasing support for greater intervention by the Government through the creation of a national asset management company that would purchase bad loans from the banks. However, there are the issues of the fiscal burden and moral hazard that such a measure can generate.

12. In addition, Mr. Singhakowin pointed to the need for further consolidation of the sector through market-based mergers and acquisition, including by foreign banks, which would entail the revision of current regulations that are restrictive in this regard.

Dialogue

13. Participants discussed the dominant role of bank financing in Thailand and the prospects of enhancing other financial institutions for financing, such as domestic bond and stock markets. Mr. Singhakowin indicated that the stock market in Thailand is currently moribund, while the bond market is still insignificant in amount of funds raised but is growing rapidly.

14. There was also discussion of whether the large-scale entry of foreign banks could transfer technology and introduce a different culture of risk management to domestic banks. Because the presence of foreign banks is still small — about 10 per cent of the sector — it is too early to judge their impact in this regard since technology can be transferred quickly but corporate culture only gradually.

New dimensions on the Asian financial crisis and lessons for domestic policy makers

15. Mr. Valdepenas highlighted the differences between the underlying risks in the Asian financial crisis and those in previous financial crises. He then drew lessons for policy makers with regard to the financial policies and mechanisms needed to manage the new risks.

16. He identified exchange rate risk and interest rate risk as the new financial risks that emerged in Asia in the 1990s. He attributed their origins to trade and capital account liberalization in the regional economies and financial globalization, which resulted in increasing international borrowing by corporations and banks in the region. Consequently, these new risks in addition to credit risk became concentrated in the private sector. Once the crisis erupted, analysis and response was full of flaws. The lack of instruments to confront it also became evident.

17. In the aftermath of the crisis, the framework for resolution of the debt overhang in the private sector is still being worked out since the issues are fundamentally different from those of balance of payments crises emanating from the public sector. The damage was deep, and countries are still coping with corporate bankruptcies and a massive debt overhang. In addition, monitoring for early warning of impending crisis under these circumstances was more difficult because of a lack of certain financial data, particularly at the sectoral or firm level.

18. Mr. Valdepenas underscored the need, therefore, for new data and analytical tools to improve the understanding and management of these new risks, including management of international reserves and monitoring of corporate debt structure. He also emphasized the need for strengthening financial mechanisms for better risk management, such as improvement of the hedging instruments for foreign exchange risk. Management of international reserves should look farther than import financing requirements to include capital account consideration. During crisis, discouraging short-term capital, particularly foreign exchange speculation (transactions that are not the counterpart of trade or a required payment), is essential.

Dialogue

19. There was discussion of the effect of "herd behaviour" among international investors on the massive withdrawal of capital from Asia. There were differing views on whether even with the appropriate information there would have been a more orderly exit of investors.

20. Participants also raised questions about the deep impact of the crisis on unemployment and poverty and the need for social safety nets. There was discussion concerning the institution of a foreign exchange transaction tax that could be increased in a crisis. There were differing views on its effectiveness as a deterrent to volatile international financial flows. Some participants believed that only a very significant tax rate could effectively change risk assessment by speculators.

Pension reform in Chile

21. Mr. Somerville presented the experience of pension reform in Chile, which was instituted after the collapse of the previous publicly administered "pay-as-you-go" social security system in the late 1970s.

22. In the previous system, the level of funding was dependent on the ratio of contributors to beneficiaries. Moreover, there was no relationship between contributions and benefits. As this ratio deteriorated rapidly in the 1970s, owing largely to demographic factors, funding declined sharply.

23. The basis of the new system put in place in 1980 is the privately administered compulsory individual contributory account, with a government guarantee. This guarantee provides a minimum level of pension to individuals with 20 years or more of contributions if their account collapses. The Government is also responsible for supervision of the system and providing incentives for savings in the voluntary account, which augments the individual's pension fund. There is, however, individual choice of the agent administering the account, the form of benefits — as an annuity or a defined schedule of payout — and age of retirement. The system currently covers 60 per cent of the workforce, with coverage of 95 per cent of employees but only 10 per cent of the self-employed.

24. Funds in the pension have grown rapidly to $35 billion, equivalent to about 50 per cent of gross domestic product (GDP), with 322,000 pensions paid out by the end of 1999. The investment allocation of the pension fund is regulated by the Government, with a substantial proportion invested in bonds issued by banks and Central Bank notes. Funds from the system have enabled banks to finance long-term loans for mortgages. A minority of the funds is invested overseas and in domestic private bonds and stocks. Returns on investments averaged over 11 per cent in real terms annually until the end of 1999. The cost of managing the funds is about 1 per cent of funds under administration. While the number of administrators is limited by regulations to eight, they are not a cartel but are regulated by the Central Bank.

Dialogue

25. There was discussion on the transition to the current system, when the Government had to take over the obligations of the previous system, which amounted to about 7 per cent of GDP and represented an onerous burden on the budget, particularly in the early 1980s when the deficit was large. Some wondered whether many developing and transition economies could

handle the demand on fiscal resources of such a transition.

26. Some participants raised questions about why the system had to be privatized and whether a restructured publicly funded system could have worked just as well. Concerns were expressed about the limited coverage of workers in the current system.

27. There was also discussion of the benefits of the new pension system. Mr. Somerville emphasized its positive impact on savings mobilization and economic growth in Chile; he attributed a large part of the rise in savings rate in Chile in the 1980s and 1990s to the implementation of the new system. He also indicated that the system has effectively channelled domestic savings to investment in domestic companies. In addition, a good working social security system is the best safety net. A similar system has been adopted or in the process of being adopted in many Latin American countries and other countries, such as Poland.

II. Foreign direct investment, project finance and venture capital

Moderator:

Asda Jayanama (Thailand), Co-Chair of the Preparatory Committee

Panellists:

Kenneth Rind, Founding General Partner, Israel Infinity Venture Capital Fund, New York

Andre Van Heemstra, Director, Unilever, Rotterdam

Beatrice Rangel, Senior Adviser to the Chairman, Cisneros Group of Companies, Caracas

Rodney Harper, Director, Alcatel, Paris

Thomas Marshella, Managing Director, Project/Infrastructure Finance, Bank Loan Ratings, Moody's Investors Services, New York

Encouraging venture capital in developing and transition economies

28. Mr. Rind outlined the growth of venture capital in the United States of America and Israel, identifying specific benefits from the industry and drawing lessons for other countries. Between 1979 and 2000, United States venture capital operations went from a $1 billion activity managed by 25 funds, with $0.6 billion invested in 300 companies, to a $120 billion industry managed by over 1,000 venture funds, holding $110 billion in 7,000 companies. The United States promoted this growth by lowering taxes on long-term investments; permitting pension funds to invest; facilitating market exits for shareholders; offering technology incentives; cutting down military spending and taxes; opening up university laboratories to collaborative research; and welcoming foreign entrepreneurs.

29. In 1986, Israel had two venture capital funds worth $30 million operating amid state socialism, government hostility to business and brain drain to the United States. It had world class military technology but just one world class commercial firm and a handful of foreign-owned research and development groups. By 2000, there were 150 venture groups managing $6.5 billion through 4,000 new companies, over 100 with international portfolio offerings overseas. The vitality of Israeli firms was reflected in acquisitions by dynamic multinationals, such as Microsoft, Cisco, Intel, Siemens and Marconi, and in investments from premier sources, such as Telecom Italia, Credit Suisse, Ericsson, Singapore and Hyundai among others. The Government promoted this expansion by directly stimulating the development of Israeli high-technology firms. Measures ranged from up-front repayable funding for new research and development, United States-Israeli seed funding for industrial projects and government start-up support for technology incubators to tax holidays and avoidance of double taxation on outside investors. The immigration of highly skilled citizens from abroad (especially the Russian Federation and the United States) was a significant boost. The important messages for Governments in other countries were: build strong educational infrastructure, encourage university-industry collaboration, promote foreign research and development activities, attract corporate strategic investors and establish policies allowing entrepreneurs to thrive.

Dialogue

30. Participants asked whether the inflow of capital from United States markets and the influx of skilled human resources from the United States and the Russian Federation did not make Israel a special case. What, in the absence of such atypical assets, would an Argentina, a Brazil or a Chile have to put in place to

jump start venture capital? In addition, was the case of India and its software industry not more relevant for developing countries? Mr. Rind acknowledged that the Russian Federation in particular had provided a rich flow of human resources, but Israel's two world class universities had also played a key catalytic role. Countries should promote university-industry partnerships and offer qualified expatriate nationals incentives to return, including research and development support, tax breaks and capital equipment support. He thought such countries as India had made considerable progress in encouraging investment in new economy industries and could do more with better incentives, for example by eliminating confiscation policies.

31. In response to questions about how activist venture capitalists are as shareholders, Mr. Rind pointed out that, typically, a venture capital fund would take a board seat on the basis of investing between one sixth and one third of equity in a firm.

Corporate criteria for investing in developing country markets

32. Mr. Van Heemstra profiled his company's business policies and criteria for investment. Unilever is a multinational, multi-local company, with deep roots in the societies in which it operates, dedicated to conducting business in a responsible and sustainable way, including stimulating local employment, helping to raise levels of education and upholding environmental and labour standards in line with global corporate policies provided that countries enforce such standards fairly.

33. He stressed that Unilever appreciates the role foreign direct investment (FDI) plays in economic development. With 95 per cent of future population growth projected to take place in developing and emerging markets, along with 70 per cent of consumption increase, the company was expecting to see up to 50 per cent of future sales and investment concentrating on developing and emerging economies. As a long-term resource, FDI creates a stable virtuous circle of wealth, by supporting jobs (directly and indirectly), building local skills, injecting technology into the supply chain and catalysing local economic activity. For example, the company employs some 6,000 people in four South-East Asian markets through operations that indirectly support another 45,000 jobs. It provides skills and sets quality standards for local managers, employees and suppliers. By focusing on its core business, Unilever increasingly outsources non-core functions to local firms, providing them in the process with technology inputs and strengthening their competitive position. Yet FDI has its limits. It can neither compensate for a weak national education system nor supply more than a relatively small proportion of gross fixed capital formation in the economy.

34. Unilever, like other companies, invests in markets which exhibit (a) political and economic frameworks conducive to efficient business, and (b) good governance and political stability. Companies expect a level playing field and fair treatment from public authorities before the law, including through strengthened intellectual property rights. They look at progress in removing impediments to effective operations (tariff and non-tariff barriers) and restrictions on ownership and trading rights. They value markets that are open and regionally integrated, with skilled workforces. They count on countries to invest in good basic infrastructure. China's forthcoming accession to the World Trade Organization (WTO) will be a critical test of how the business and developing worlds can meet on new common ground. Ultimately, however, the right political and economic framework is a necessary but not sufficient condition. What firms most closely look for are growth potential and good rates of return. International investors will go where the balance between risk and return looks best.

Dialogue

35. It was suggested that the speaker had portrayed investment decisions as they might apply to doing business in, for instance, the Netherlands. Are investors prepared to go further to increase the scope for investing in developing and emerging markets? What extra steps would they take to develop host economies? A second participant asked whether a company could be a good corporate citizen alone in situations where its competitors were less constrained by their corporate ethics. Is it not time to consider some standard codes of conduct and international investment agreements to make good corporate citizenship more than voluntary? A third participant agreed that Unilever is known for its ethical business vision but asked to what extent the company institutionalizes its vision in the investment guidelines of its pension funds, which account for tens of billions of dollars in investment.

36. Other participants observed that the most critical determinant of FDI is often sheer market size, as illustrated by investor concentration on such countries as China and Brazil. It was asked under what circumstances Unilever invests in small markets. One or two commentators returned to the point that investors appear largely preoccupied with the supply side of FDI. FDI levels had increased but only for a few countries. For the more than 50 poor developing nations with good track records in economic reform and governance yet without significant FDI, the issue is how to shape the supply side to strengthen their absorptive capacity and thus increase demand. How, for example, could poor countries invest in infrastructure to attract investors in the absence of resources and available official development assistance (ODA)? Some way to break this vicious cycle and deepen the investment process must be found.

37. Mr. Van Heemstra underlined that Unilever does not take the hospitality of host developing countries for granted, illustrating his reply with reference to recent company activities in Viet Nam. Unilever remains committed to maintaining a positive dynamic with local small and medium-sized enterprises and to displaying corporate social responsibility in respect of local training, skills development and technology diffusion, as well as in matters of public safety, health and environmental standards. The motive for this approach is not charity but the practical recognition that businesses prosper in societies that prosper. On the question of widening corporate citizenship, the answer does not lie in restrictions imposed from outside. Social responsibility has to be an internal ethic voluntarily adopted by firms and discharged with conviction.

38. On guidelines for pension fund investments, Mr. Van Heemstra observed that such funds have only recently been liberalized and are still evolving their own investment criteria. Fund managers have different responsibilities and it is not possible to enforce a corporate vision on them. Market size, he acknowledged, is often a key factor for investors, and by going into large markets, such as Indonesia, Unilever captures economies of scale, leading to cheaper products for more people. Some small markets are attractive for other, operationally oriented reasons, and more could become so through policies of regional or subregional integration. In terms of deepening the investment process, Unilever does not consider the 7,000 jobs created in Viet Nam or 13,000 in Indonesia to be negligible for the people concerned. Nor should the other stimuli to local economies he had mentioned be overlooked. There is, however, a central challenge for the global community to address in helping poor countries to participate more equitably in globalization and its benefits, including FDI. This is a challenge that all sectors must consider and address together.

39. Lastly, one participant noted that while Unilever advocates good governance for countries, it apparently prefers self-regulation for corporations. What criteria does the company apply to social or environmental impact assessment, what auditing practices does it follow and how does it independently verify that community and shareholder interests are served?

40. Mr. Van Heemstra replied that when a company generates internal enthusiasm to live up to social and ethical responsibilities, the results are more effective. However, Unilever does actively underwrite its financial, social and environmental accountability through independent audits and through community-oriented thematic projects around the world in sustainable fisheries, sustainable agriculture and clean water development. It has also convened an internal environmental council and published occasional studies on its web site of how the company is living up to its statement of purpose.

Attracting FDI in developing countries

41. Ms. Rangel addressed what it takes to succeed as a private direct investor in emerging markets and what conditions facilitate FDI. Host country markets demand choice, quality, consumer rights protection and technology innovation. They expect products relevant to their needs and attuned to local markets. New investors should conduct a comprehensive dialogue with employees, stakeholders and society at large to explain their goals, opportunities, costs and time frames. Realism is important in clarifying expectations to partners. Employee incentives should be provided in the form of stock options, bonuses and most of all training, which is critical in the service sector.

42. Companies should listen to communities, allay their fears about change, and help them gear up to cope with the new economy. Education, especially in information technology (IT) skills, is a major popular priority. Business-government partnerships could help communities to catch up.

43. Outside investors expect macroeconomic stability, chiefly a stable currency and labour market, strong, effective government, competition policies ensuring a level playing field, evidence of institutional development, peaceful solutions to social challenges, and laws protecting consumers and investors. Investors look for good human capital and knowledge, which could be developed by building up local IT structures and deepening Internet penetration. The experience of the Cisneros Group of Companies shows that education is the most effective investment that both companies and Governments could make, and Ms. Rangel called on the World Bank, the Inter-American Development Bank and Governments to form partnerships for human resources development.

Dialogue

44. A number of questions were posed, including how decisive it is for developing countries to have competition policies given that some investors seek monopoly positions in local markets; how could FDI contribute more to the global financing for development agenda, especially in smaller countries, considering that today some 12 countries receive 80 per cent of all inflows, with more than 50 per cent going to only two big players, China and Brazil. The former had neither a competition policy nor significant consumer protection; how does the Cisneros Group define labour market stability? A free environment for trade unions? Dialogue with stakeholders?

45. Participants noted as well that while market size was evidently important, some smaller markets receive more FDI per capita. The challenge is to use technical assistance through intermediaries with proven private sector development experience in smaller countries, such as the International Finance Corporation (IFC), to build up their attractiveness to investors. It was pointed out that local human capital is essential to the quality, as well as quantity of investment. Participants also asked whether the Cisneros Group could illustrate some of the qualitative gains in terms of education, human rights and public freedoms, and whether increasing national capacity to manage local domain registrations for Internet expansion is a top priority in helping countries to benefit from the information revolution, which is changing the nature of property and wealth.

46. In response, Ms. Rangel replied that competition is key to protecting consumer choice and building local equity and trust, noting the long-term benefits of a country being able to choose, for example, between land-based and satellite telecommunication installations. She admitted that size undeniably makes China an attractive self-contained market, but felt that smaller countries could also earn their way by providing goods and services for the global economy. She stressed that a stable labour market is one where countries do not change the rules every day and companies make long-term commitments to human resources development. Two illustrations of FDI-related social investment in education came to Ms. Rangel's mind. By using free transponder space on the DirectTV satellite service for distance education, 2,000 teachers in rural areas of Latin America are upgrading their skills on the back of the entertainment industry. In addition, the Cisneros Group sponsors a non-commercial education channel that reaches 37,000 Latin American schools every day.

47. Ms. Rangel also accepted that there is scope to use technical assistance through a variety of sources, in addition to the World Bank and the Inter-American Development Bank (IDB), to empower educators, communicators and others and create an enabling environment for FDI, and that the provision of resources and know-how to develop information and communication technologies is a major priority for developing countries and is best managed through public-private partnerships.

Investing in technology in developing countries (bridging the digital divide)

48. Mr. Harper recalled that bridging the digital divide has been a top priority for decision makers at the Okinawa Group of Eight Major Industrialized Countries Summit. With 1 in 2 Internet users online in the United States compared to 1 in 250 in Africa, the scope for development was clear, notwithstanding some developing country worries about information security. The way forward is not to duplicate Internet applications as used in the North, which serves only niche markets in the South. Rather, it is to make the Internet a prime economic development tool, offering relevant end-user services and compensating for the lack of certain infrastructure (e.g., in transport, health, food supply and logistics). Mr. Harper illustrated this point with reference to a range of web-based neighbourhood end-user services in developing countries, and went on to suggest some key factors for

broader Internet take-off, including dedicated broadband access, much wider dial-up access and information content with strong local added value. Partnerships are another key factor. Governments, service and content providers, financial institutions, suppliers, NGOs and the United Nations should come together to generate project finance and create value-adding products in this major growth area. He noted that new entrants to the information and communications technology market have their own funding capabilities, and local private partners are strongly motivated to form start-ups.

Dialogue

49. One participant noted that information and technology initiatives, such as the Info-kiosk project in India, have shown that telecommunication networks could potentially address a very broad range of development needs in health, agriculture and other sectors. The challenge faced by active United Nations agencies, such as the United Nations Development Programme (UNDP), is how to scale up such initiatives. How could the financing for development process help focus attention on this specific challenge? Two participants asked what telecommunications firms expect from developing countries, for instance, by way of reducing barriers to wider Internet deployment in their societies, and what they expect from the United Nations.

50. Mr. Harper replied that the key answer is to take a partnership approach. The necessary factors for success are political will, well defined, sustainable projects, project financing and a willingness to share risks. Such companies as Alcatel are in technical design and operations. They need to be connected to Governments and other actors. The United Nations role is to bring prospective partners together as an honest broker in order to exchange contacts and ideas, facilitate discussion and promote a common mindset. Such players as the World Bank could build confidence in information and technology projects by participating directly themselves.

Debt financing of projects and infrastructure in emerging economies

51. Mr. Marshella explained that his specialization is project finance, not sovereign risk assessment. Debt-financed project analysis is a relatively recent discipline, focusing on guarding against the downside through independent judgement at a time when global demand (1 to 2 trillion dollars) far outstrips supply. Private investors supply about 71 billion dollars of such debt financing. These investors became central players when, during the buoyant mid-1990s, for various reasons emerging markets looked outside for capital. He went on to characterize the experience of debt investors, primarily United States institutional investors in loans and bonds, since then.

52. Some 70 per cent of Asian project debt rated during the mid-1990s has either been downgraded or had its outlook revised downward by Moody's. Exactly half defaulted and of those that have not, only one is still rated investment grade. Project and infrastructure investors have since moved on to more mature economies, which have sought private debt capital inflows via asset sales and the restructuring of monopoly industry (e.g., electric power). These investors evidently perceive better risk-reward ratios outside of emerging economies.

53. Several factors account for this. Most debt-financed projects in emerging markets are denominated in local currency and are thus vulnerable to currency swings and devaluations. As Asian market fundamentals have weakened, opaque embedded risks that were once hard to monitor have emerged and exchange rate risks have predominated, changing investors' perceptions and eventually causing them to depart. Today, hedging instruments are sought to counteract risks, but there remain questions how to finance projects going forward on this basis. It is also necessary in any emerging market to understand the important role of legal infrastructure to protect creditors' rights. Investors are not averse to a level of risk, but the key question is to identify exactly where such risks reside and what can be done to reduce uncertainty. This is not possible in the muddy situation beforehand. These basic challenges must be addressed if private capital is to flow back to emerging market projects.

Dialogue

54. Discussion centred on the following questions:

(a) How should the international community bridge the gap between the United Nations world, which speaks of such goals as halving extreme poverty by 2015, and the world of finance, which emphasizes the complexities and high risks involved in doing business in developing countries? What two or three concrete measures should governments focus on to help reduce uncertainty and close the gap?

(b) Since it is clear that the transcendent quality of private capital movements puts it beyond government capacity to manage uncertainty, is there a way to encourage those who assess profitability to take a longer-term view of risks? Should not the opportunity costs of failing to provide financing to poor countries also be assessed?

(c) As there are questions about the objectivity of country ceilings established by debt financiers, is there a need for international standards to ensure that project risks are correctly assessed, as well as a global body to oversee those standards?

(d) Would not the cancellation of unrepayable developing country debt help lower uncertainty? Would ratings agencies oppose or support such cancellation?

(e) Should not such national assets as gold or valuable commodities (oil) be weighed positively when making risk assessments?

55. One participant observed that when a ratings agency, such as Moody's, says "no", it simply means that a project cannot be financed on commercial terms. Projects can in fact be financed as constructs from multiple sources through a range of instruments, from grants through to full commercial loans. Moody's could offer countries a project analysis service to expose the weaknesses that other forms of finance are needed to address. It could also rate NGOs in the microcredit business to help them qualify for mainstream capital financing.

56. Mr. Marshella observed that, for investors, ratings are just one indicator. Ratings agencies are not arbiters. They provide reality checks, not endorsements of national policy. On the assessment of opportunity costs, it has to be grasped that debt financing is a contractual obligation and that investors want certainty. Time horizons for returns are not invariably fixed and, depending on other factors, could be longer term. On offsetting currency risks by putting aside valuable commodities (oil or gold), he agreed that this might be factored into certain projects that had structural integrity provided that the commodity was denominated in the same currency as the loan. On the correctness of risk assessment, he pointed out that agencies rate risk on a relative as well as absolute basis and that country ceilings are a relevant factor. Agencies also provide the market with supplemental information that investors additionally consult. On such issues as debt cancellation, he stressed again that ratings agencies do not look to endorse particular policies or recommend special measures, which are the domain of Governments. They would, however, be glad to help countries to appraise the risks associated with project constructs along the lines previously suggested by one participant.

III. Other private capital flows

Moderator:

Ambassador Jørgen Bøjer (Denmark), Co-Chair of the Preparatory Committee

Panellists:

Cheryl Hesse, Senior Counsel, Capital International, Los Angeles

Francesco Anania, Associate Director, Structured Finance Department, Medio Credito Centrale, Rome

Yoshiyuki Fujisawa, Chairman of the Board of Directors, Industrial Bank of Japan, Tokyo

Hanns Michael Holz, Head of Global Public Affairs, Deutsche Bank, Frankfurt

Corporate governance in emerging markets: an investor's perspective

57. Ms. Hesse referred to corporate governance as the interlocking sets of laws, regulations, corporate codes and judicial systems that govern the relationships among shareholders, directors and managers of corporations. Corporate governance codes or best practices guides have been adopted by many organizations, from stock exchanges, such as the Stock Exchange of Hong Kong, and intergovernmental organizations, such as the Organisation for Economic Cooperation and Development (OECD), to institutional

investors, such as the California Public Employees Retirement System. These codes identify three key characteristics of good corporate governance: transparency, equitable treatment and accountability.

58. Corporate governance has important implications for emerging economies, because the emphasis on good corporate governance appears to be spreading among investors as well as diverse groups around the world, such as the Asian Corporate Governance Forum, the Kenyan Private Sector Initiative for Corporate Governance, and the Republic of Korea's Participatory Economy Committee — People's Solidarity for Participatory Democracy. Germany has created a stock market that limits listings to companies that adhere to certain principles of corporate governance, and Brazil is investigating doing the same. And over 330 participants from 25 countries attended a meeting of the International Corporate Governance Network held in New York in summer 2000.

59. Several factors have contributed to the current emphasis of corporate governance, including the increase in privatization and the 1997 Asian financial crisis, which spread to other emerging markets. In many privatization instances, the liberalization of financial systems seems to have outpaced the development of sound corporate governance practices. The financial crisis that began in Asia in 1997 highlighted the risks of investing in countries with poor corporate governance. Individual companies failed, in part due to weak capital market regulation and failure to protect minority shareholders. These individual failures created uncertainty that quickly contaminated confidence in entire countries.

60. International investors have cooperated with developing nations' Governments to encourage reform. This mutual effort is an integral part of the globalization of world markets that both investors and developing countries will need to address.

61. Large investors in emerging economies, such as Capital International, are becoming more involved in highlighting the need for corporate governance reform. They recognize the need for continued and expanded dialogue on the issue of corporate governance — not only in emerging markets but also in developed markets. They also recognize that there is no single set of principles that will work for all nations: corporate governance reform must be undertaken within the context of local conditions, giving due regard to a country's corporate history and culture. While remaining committed to the process of improving corporate governance, they will also invest their clients' assets with due regard to the potential risks that corporate governance lapses bring.

Dialogue

62. Several interventions focused on the importance of corporate governance, including as a measure to reduce the cost and increase the supply of capital in developing countries. However, it is not a panacea for solving important needs of developing countries. Globalization of markets does not go hand in hand with globalization of opportunity, and the challenge is to harness equal development of both. In addition, the corporate governance field is still in evolution even in developed economies, with social responsibility increasingly taken in consideration, at times at the request of clients. For instance, the California Public Employees Pension Fund, a large United States pension fund, has recently introduced human rights conditions to its international investments. Still, economic and financial considerations remain the critical parameter for investment decisions. Debt cancellation is an example of shareholders' interests uneasily squaring off with stakeholders'.

Private capital flows to developing countries

63. Mr. Anania mentioned that Medio Credito Centrale (MCC) operates both as an investment bank specialized in project and export finance and as a development bank managing all concessional loans to developing countries on behalf of the Italian Government. Mr. Anania described different ways, illustrated by concrete examples, in which MCC's dual role can stimulate foreign investments to developing countries.

64. As an investment bank, MCC executes both project finance and corporate finance operations. The former activities generally involve large investment projects in selected sectors, such as infrastructure, energy, petrochemicals, telecommunications and environment. The contractual structure of these transactions aims to spread risk evenly among project participants (public sector, private investors, lenders, contractors, purchasers, suppliers, operators). A successful project can attract private flows in the form of equity from shareholders and private investors; bond issues from the private market; and subordinated loans

and standard commercial loans from the lenders. Mr. Anania illustrated these types of project with the examples of a steel factory in Egypt, a power plant in Pakistan and a power plant in Morocco.

65. The second type of operation — corporate finance — can attract private flows to developing countries mainly in the form of equity underwriting and loans. These transactions involve fixed investments carried out by medium-sized firms, in the form of a joint venture, mainly in the manufacturing sector (mechanical, textile, wood/paper etc.). The typical case entails Italian medium-sized companies that intend to expand the market of their products overseas and to invest in a company that has strong local roots. In such cases, the Italian company initially purchases a block of shares; subsequently, it restructures the business through technological revamping, which is generally financed with new equity and debt. MCC has provided financing to many such projects in developing countries, especially India and China.

66. MCC also manages the Italian Government's concessional loans to developing countries. These funds help to finance public and private initiatives included in the framework of multilateral long-term programmes implemented by the respective Governments. In the last 20 years, MCC has provided on behalf of the Government of Italy more than 450 soft loans for a total amount of about US$ 7 billion, mainly for public infrastructure projects. In the last few years, a new type of credit line has been used to promote private investment by small/medium-sized firms. Industrial and agribusiness projects in particular have been financed in the form of joint ventures.

67. These credits are granted to local central banks, who subsequently on-lend them through the local banking system to the mentioned joint ventures on very favourable loan terms. These facilities, recently granted to Tunisia and Egypt, among others, have been very successful and many Italian companies have invested equity to establish joint ventures.

Lending to emerging markets: a banker's perspective

68. Mr. Fujisawa promoted the Japanese model as a high saving, stable, diligent and socially equitable country. He identified two main drawbacks to applying the Japanese model to developing countries. First, countries are highly dependent on capital flows; second, capital flows are today very volatile, so that efforts at regional cooperation in this area are required.

69. Among the conditions to successfully attract foreign capital, Mr. Fujisawa underscored the importance of sound financial practices and good corporate governance. In addition, efforts to foster domestic financial markets are required to raise long-term funds. Solid risk and return analysis is also very important.

70. Moreover, the private sector needs enabling conditions, including accountability, transparency and stability, to invest in developing countries.

71. Both private and public financing are critical to achieving sustainable development in developing countries, and they complement each other. Japan is proud to be the largest single provider of official development assistance.

Dialogue

72. International Monetary Fund (IMF) conditionality was perceived by some NGO representatives as putting corporations from developed economies at an advantage against developing countries' citizens; for that reason as well as for its questionable impact, it should be lifted.

73. Capital controls imposed by developing countries remain a controversial policy instrument, even in emergency situations, in the view of participants. They represent an additional cost for investors, which needs to be factored in their risk/return analysis and would create an incentive to shift assets elsewhere.

Deutsche Bank: corporate citizenship in emerging markets

74. Mr. Holz stressed that Deutsche Bank recognizes the importance of the developing world to both its current and future success, as well as the responsibility of multinational companies to facilitate the development of local capacity and viable civil society organizations in developing countries.

75. The realities of globalization offer a unique opportunity to effect positive change, encourage sustainable communities and develop stable societies. Globalization's promise cannot be realized, however, unless globalization results in broad benefits for the majority of the world's people, especially those living outside the economic mainstream. Not only is this a

moral imperative but it is also a necessity. In the short term, it is certainly in companies' own interest to work to counter the mounting and well organized grass-roots backlash against globalization. In the long term, perhaps the most compelling argument for the involvement of companies is their own survival. To maintain the economic growth that fuels the expansion and growth of businesses, they must remove the barriers of poverty and ignorance that isolate much of the world's people from the marketplace and access to economic independence and prosperity.

76. Deutsche Bank believes its role in society must be one that helps to buffer the impact of change on the most vulnerable. To this end, Deutsche Bank established the Deutsche Bank Microcredit Development Fund (DB/MDF), which aims to provide subordinated debt to local microcredit programmes that can serve as collateral in leveraging local domestic bank borrowings.

77. Conventional relationships with domestic commercial banks are an essential step to freeing microcredit programmes from their dependency on donor aid. DB/MDF currently has loans in place supporting microcredit programmes in Chile, Mexico, South Africa, India, Pakistan and Colombia.

78. Deutsche Bank's commitment to sustainable development goes beyond contributing to poverty alleviation through microcredit, focusing also on strict environmental compliance and renewable sources of energy. Deutsche Bank is proud to be part of several networks with similar objectives, including the World Business Council for Sustainable Development, the UNEP Financial Services Initiative and the Secretary-General's Global Compact.

79. Deutsche Bank's philosophy is: "Think global, act local". It reflects the belief that while different markets require different methods and approaches, issues are often similar across countries.

Dialogue

80. The promotion of small and medium-sized enterprises in developing countries was a concrete step offered as an example by MCC, towards accelerated growth in the local economy, poverty eradication and reduced inequality.

IV. Trade, systemic and other issues

Moderator:

Asda Jayanama (Thailand), Co-Chair of the Preparatory Committee

Panellists:

Kamal El-Keshen, Deputy Director, African Export-Import Bank, Cairo

Marshall Carter, Chairman, State Street Corporation, Boston

Thomas M. T. Niles, President, United States Council for International Business, New York

Mthuli Ncube, Chief Executive Officer, Barbican Asset Management, Harare

Trade issues relevant to Africa

81. Mr. El-Keshen pointed out that exports as a share of GDP have stagnated in Africa. Poor export performance is linked to inadequate access by countries to imported inputs, which in turn is linked to inadequate financing. This completes the vicious circle: without exports and with declines in ODA without any increases in private flows, the finances will have to come from export revenues. Given the vital role of exports, therefore, a way has to be found to urgently encourage growth in the African export sector.

82. There are many debilitating characteristics of African exports: they are concentrated in a few products, dominated by tropical beverages (coffee, tea, sugar etc.), are highly commoditized and are sold to a few OECD markets, mostly those with which the exporters have had colonial histories. Exports are largely unprocessed, with low value added and limited demand growth possibilities.

83. They tend to have low technology inputs and low processing. All of these in turn lead to low export production, and therefore to low export-GDP ratios. In addition, intra-Africa trade, which has enormous possibilities, is negligible.

84. With the changes in the global environment, new problems have also arisen: many African countries have dismantled their export marketing boards but have not found adequate substitutes. With the emergence of new entrants, risks have increased and access to finance is limited now that the old marketing boards no longer exist.

85. Mr. El-Keshen enumerated several strategies for enhancing growth prospects for Africa:

(a) Create a stable macroeconomic environment, including a sound exchange rate policy;

(b) Attract foreign direct investment, which would help to (i) increase export production; (ii) alter the nature of exports, including increasing technological inputs and processing (value-added); (iii) provide lucrative market contacts; and (iv) strengthen management skills;

(c) Ensure that the current conventional wisdom of privatization and government withdrawal from financial sector issues does not mean government abdication of its responsibilities, including the creation of an appropriate regulatory environment, with clear penalties for non-performers;

(d) Attract the right kinds of finance, including venture funds.

86. Mr. El-Keshen concluded by identifying the Africa Growth and Opportunity Act and the European Union's Cotonou agreements as important for providing market access, and noting that market diversity is important if export production is to increase, and that WTO rules should be revisited to enable African countries to join with less stringent rules so that they can take advantage of the opportunities provided. Article 27, in particular (on subsidies and countervailing measures), should be expanded to cover more African countries.

Dialogue

87. The discussion that followed focused on the following main areas:

(a) Inability of African countries to attract the types of production that Asian countries have been able to capitalize on: the concern was expressed that such production was usually linked to exploitative labour practices. Mr. El-Keshen responded that Africa has not been able to provide the working environment that would enable low-cost production of goods at international standards;

(b) The Africa Growth and Opportunity Act and whether it offered concrete opportunities for growth: the question was posed whether the African Export-Import Bank can help support countries in their efforts to build strong private sectors, including help in taking advantage of such agreements, enterprise development, which is critical to export production etc. Mr. El-Keshen indicated that, unlike the development banks, African Ex-Im Bank is a commercial entity with mixed membership from central and commercial banks; it started only in 1994, focusing on short-term lending (less than one year) of about US$ 1.6 to 1.7 billion; and its primary focus is to support exports (rather than imports) in African, Caribbean and Pacific countries. He added that there are many innovations (export business zones or units, for example, with improved infrastructure and regulations) which have been used successfully in some countries to support exports. He concluded by saying that the African Ex-Im Bank had close ties with the African Development Bank (which has a special seat on the African Ex-Im Board) and that the African Development Bank is the best locus for development activities, including technical assistance and capacity-building.

Investing in emerging economies

88. Mr. Carter spoke about trends in demographics and the financial world, and how these trends might impact investing in emerging markets. He began by providing some background information on his institution, State Street Corporation, which 25 years ago was a regional bank taking deposits and making loans to corporate clients in New England; today, the Corporation is a global company that combines information technology with banking, securities processing, investment management and trade execution. It delivers these services to customers in 92 markets around the world, with over 17,000 professional staff employed in 23 countries; it holds $720 billion in customers' assets under its management and over $6.2 trillion in its custody; and touches roughly 13 per cent of the total world market for stocks, bonds and securities of all kinds every day, a market that is estimated at well over $50 trillion in assets. He covered the role of custodians in settling trades, safekeeping securities, keeping records and a host of related tasks which make the financial markets work.

89. He then discussed shifts in stock markets in the last two decades: the number of investable stock markets have doubled since 1980, from about 83 in 1980 to over 160 today, and the major global custodians routinely cover about 90 of them. This means a tremendous amount of cash and data flow,

giving custodians a sophisticated understanding on what is happening in the markets. And some of these trends have implications for investment in developing nations.

90. Some of the trends he mentioned include the shift to global capital markets finance and how developing economies can access these markets; the movement from "geopolitics" to "geo-economics"; and the advent of technology and the Internet. These are described in detail below.

The shift to global capital market-based finance

91. Global capital markets have been displacing traditional banking as the key intermediators between providers and borrowers of capital. Therefore, there is clearly enormous room for further growth of stock and bond markets in continental Europe, Asia and across the developing world.

92. The key advantage of capital markets is that, together with the derivative markets for options and futures, these markets can minimize risk (i.e., can hedge and distribute that risk widely). Countries must act soon to spur the growth of capital markets that can, in turn, finance new economy industries. But these countries also have the obligation to protect the investor.

How can emerging markets capitalize on these trends? What needs to be done?

93. Prerequisites: prior to the crisis of 1997/98, investors were attracted to emerging markets by a combination of impressive rates of economic growth and government incentives. But that has changed — institutional investors today decide whether to invest in emerging markets based on a number of factors, not just promised rates of return. Therefore, to be players in the new global economy, developing economy nations need to take action to provide confidence to investors and markets, including increased financial disclosure under internationally recognized accounting standards; globally acceptable legal frameworks; improved debt management practices; coherent bankruptcy codes and financial market supervision; more market-based, less relationship-oriented banking systems; sound macroeconomic polices; and sustainable currency exchange regimes. With such reforms, emerging markets can mobilize domestic savings and attract far more in both direct investment and portfolio flows than they have ever received in foreign aid.

94. The key to success for emerging markets is the creation of a level playing field, which is only possible when there is freedom from government interference, as well as complete transparency — meaning that the books and records, ownership, revenue streams, expenses and everything related to the financial performance and ownership of companies are open and clear for all to see.

Moving from geopolitics to geo-economics

95. The world is (hopefully) moving away from military competition and warfare towards a common quest for prosperity and growth. This movement towards geo-economics is being driven by the growth and integration of the world's capital markets; the rise in world trade — which has been outpacing the growth of domestic economies for decades; the increasing irrelevance of national borders as regulation is liberalized and tariff and non-tariff barriers disappear; and technology's ability to leverage knowledge and talent worldwide.

96. Institutional investors, such as pension funds, are leading the trend to cross-border investment; and cross-border capital flows to emerging nations already dwarf all official foreign aid by a factor of roughly six to one — $240 billion a year versus $40 billion. Part of this shift is due to declining official foreign aid — due in no small part to "donor fatigue". But the bulk of new private capital flows to developing economies is simply due to the vast new pools of capital available today.

Technology and the Internet

97. The Internet's future growth prospects are enormous in the developing world, and it can help developing countries take advantage of the major trends in global finance once the challenges of providing widespread access are met. It will force a more profound restructuring of capital markets in the next few years; it will link stock and bond markets nationally, perhaps even globally, and dramatically lower trading costs. And it will level the playing field by providing a wealth of information and analytical tools to ordinary people as well as to institutional investors.

The politics of globalization

98. Trade and investment are "win-win" transactions for national economies, but there are impacts on displaced workers and there are legitimate concerns about labour rights, the environment and cross-border investment flows. In developed nations, the global economy is often viewed with suspicion — as evidenced by the public demonstrations at recent trade meetings in the United States. In emerging markets, there is plenty of room for exploitation, and they need to develop the legal, financial, and technological infrastructure necessary to access these tremendous new pools of capital. A global economy that benefits all is within reach but is by no means inevitable.

Dialogue

99. The discussion was focused on the following main points:

(a) Debt: there have been discussions about avoiding the differential treatment of private versus official creditors (such as the Paris Club) by making all creditors of a country equally responsible for the debt workout. There is also a clear need for more comprehensive and sophisticated information of specific country characteristics. Mr. Carter responded that an early warning system that enables debt restructuring to take place well before crises hit should be available for debtor countries;

(b) Volatility: the problem of controlling volatility driven by "hot money" was raised and elicited the response that there should be restrictions on investment that is purely speculative in nature, though the challenge will be on how to do this in a workable manner; there are various available models, which have had varying levels of success;

(c) United Nations role: one participant asked whether companies are willing to come under a United Nations umbrella, to which the answer was that leadership by the United Nations regarding global financial systems is more that of leadership by persuasion than by fiat.

Global trade policy issues relevant to financing for development

100. Mr. Niles spoke about the fact that, given that development assistance is unlikely to increase, increases in exports and enhanced foreign direct investment are needed to narrow the global gap between the rich and the poor countries.

101. In the Uruguay Round of multilateral trade negotiations, the attempt was made to provide special and differential treatment to countries, but this has led to dissatisfaction on the part of developing countries regarding implementation issues. If there is a new round in 2001 after the failure in Seattle (due, Mr. Niles said, to country incompetence rather than to civil disobedience disruptions), the developed countries will have to show tremendous leadership in dismantling agricultural protection in the United States and in changing the Common Agricultural Policy in Europe. Implementing phase-out of the multi-fibre agreement is in question since developing countries are not gaining what was promised. This phase-out may, however, have the unexpected result of one country (i.e., China) dominating the textile sector in all markets. Commissioner Pascal Lamy, Mr. Niles noted, had recently proposed that the European Union should be willing to remove restrictions on all but arms imports from the least developed countries — though this was a heroic gesture, this would prove difficult to implement.

102. While underscoring the importance of labour and environmental standards, Mr. Niles stated that they should not be used in WTO as a way of maintaining protection. He indicated that the African Growth and Opportunity Act, in spite of its limitations, still represented an important first step. He recommended that countries adopt the OECD principles of corporate governance and eliminate the corruption and bribery rampant in many countries.

Dialogue

103. Following Mr. Niles' presentation, discussion was centred on the following:

(a) Labour and environmental standards: how far do the voluntary adoption of labour, environmental and human rights standards by corporations actually change their conduct — does it work for development? Mr. Niles responded that the standards are very important, but he advised going through the proposed International Labour Organization (ILO) conventions. He also noted that with increased economic development, these standards are more likely to be adhered to;

(b) Assistance to African countries to take advantage of the African Growth and Opportunity Act:

although the Act does not specifically finance assistance to countries, there are other supplementary programmes (bilateral and others) that could help;

(c) Unilateral market access agreements: it was noted that arrangements between individual countries and the developed world on market access have undermined the possibility of having such negotiations take place under WTO. Mr. Niles responded that it is often in the interest of the developed country partner to enter into these arrangements unilaterally, but that the way to resolve this is to proceed to a new multilateral trade round.

104. Additional questions and comments focused on:

(a) Protectionism in the developed world: Mr. Niles believes that it is more a political issue than a "national security" one. He also pointed out that in the United States the beneficiaries of these protections are large farmers and producers, not small ones;

(b) Market access and the Multilateral Agreement on Investment: concerning how countries can be helped to take advantage of market access, Mr. Niles responded that the Agreement is generally among OECD countries, which generally do not disagree on investments. The issue is to have workable arrangements between OECD and the rest of the world. There was some discussion about adding investment to WTO terms of reference, but it was felt that that would not be well advised. On market access, one participant commented that perhaps it would be more advantageous if developing countries could be encouraged to diversify their export base to avoid overwhelming the few sectors protected in developed countries. Although Mr. Niles agreed, he also pointed out that diversification usually comes as a result of economic growth;

(c) WTO imbalances: in response to a question on international good governance and the United Nations role in negotiating global norms, principles and standards for the private sector, Mr. Niles pointed out that the United Nations cannot play an enforcement role (since international business would reject this), and suggested that it play a more visionary role, one that promoted codes of conduct.

Financial regulatory environment in Africa

105. Mr. Ncube focused on a few points regarding the financial regulatory environment in Africa, as summarized below.

106. Stock markets have done well. For example, the Zimbabwe Stock Exchange earned 1,000 per cent in real dollar terms in seven years. Africa has small stock markets, generally illiquid, with limits on foreign currency in most countries; there are very few bond markets, with only the South African one being sizeable. The cash and money markets, therefore, are where most of the money is.

107. Banking systems are where the financial problems reside: a huge percentage of loans are non-performing, constituting on average 60 to 90 per cent on the balance sheet, where 30 per cent is usually seen as the limit. These non-performing loans have weakened the banking sector, which is normally characterized by one or two large banks that dominate more than 60 per cent of the market. This, however, can also be seen as a great opportunity for foreign bank involvement.

108. Governments are often heavily involved in the banking system, which creates room for corruption. Again, this can also be seen as an excellent opportunity for privatization. Deposit protection is important, but it is very early in the development stages in most African countries, and most banks are still in the "too big to fail" category (i.e., they will have guaranteed government bail-out because of their dominance in the market). In many countries, central banks regulate the banks that are licensed by the Ministry of Finance — this makes sanctions of banks almost impossible, particularly where there is corruption.

109. Informal credit, on which the informal sector is based, often outstrips formal credit in many African countries. Yet financial institutions have not found a way to tap into that market.

Dialogue

110. In the discussion, the questions centred on the following points:

(a) Licensing versus regulation of banks: when asked whether central banks or ministries of finance were the preferred agency, Mr. Ncube replied that this depends on individual circumstances, but highlighted the importance of having independent central banks

and of putting both licensing and regulation functions under one agency, be it the central bank or the ministry of finance;

(b) Liberalization: when asked whether liberalizing the capital account would help increase stock market flows into Africa and what types of financial infrastructure could help in this regard, Mr. Ncube discussed the importance of central depository systems that are being put into place to ensure that the existing stock markets are up to standard;

(c) Currency risk: Mr. Ncube stated that the currency risk in Africa is very high, but pointed out that the successes of the Zimbabwe stock market (1,000 per cent returns in seven years in real dollar terms) still left a sizeable profit after currency risks were taken into account;

(d) Capital controls: Mr. Ncube found that capital controls made no sense since the monies are not coming into Africa anyway. It is true that currencies take an initial knock, but they do stabilize and the funds are then available to spur growth;

(e) Regional stock markets: Mr. Ncube found that currency translation between countries is unworkable, so that he favours the option of cross-listing companies between neighbouring countries (which is currently being done in a number of African countries);

(f) Donor/taxpayer fatigue: when a participant commented on the lack of confidence that taxpayers in developed countries have regarding past development assistance, Mr. Ncube was not surprised. He asserted that this is because donors are focusing on Governments whereas they should be dealing with the private sectors of African countries.